



# **THE BULGARIAN ECONOMY**

IN THE FOURTH QUARTER OF 2003


IN FOCUS: THE BULGARIAN  
ECONOMY IN 2003

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REPORT BY  
**THE CENTER  
FOR ECONOMIC  
DEVELOPMENT**

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*The Center for Economic Development (CED) is a Bulgarian non-governmental research institute in the area of economic policy, established in 1997. Its goal is to support the economic development of Bulgaria through encouragement of public debate on economic issues and development of economic policy options.*

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## ABBREVIATIONS USED

AD.....	JOINT-STOCK COMPANY
AEE .....	AGENCY FOR ENCOURAGEMENT OF ENTREPRENEURSHIP
BAAT .....	BULGARIAN ASSOCIATION FOR ALTERNATIVE TOURISM
BAIT.....	BULGARIAN ASSOCIATION FOR INFORMATION TECHNOLOGIES
BAS .....	BULGARIAN ACADEMY OF SCIENCE
BASSCOM.....	BULGARIAN ASSOCIATION OF SOFTWARE COMPANIES
BATA.....	BULGARIAN ASSOCIATION OF TRAVEL AGENCIES
BCC.....	BANK CONSOLIDATION COMPANY
BCCI.....	BULGARIAN CHAMBER OF COMMERCE AND INDUSTRY
BDU .....	BULGARIAN DOCTORS' UNION
BHRA.....	BULGARIAN HOTELIERS' AND RESTAURATEURS' ASSOCIATION
BIA.....	BULGARIAN INDUSTRIAL ASSOCIATION
BIBA.....	BULGARIAN INTERNATIONAL BUSINESS ASSOCIATION
BNB .....	BULGARIAN NATIONAL BANK
BNR.....	BULGARIAN NATIONAL RADIO
BNT .....	BULGARIAN NATIONAL TELEVISION
BRC .....	BULGARIAN RED CROSS
BRS .....	BULGARIAN RIVER SHIPPING
BTC .....	BULGARIAN TELECOMMUNICATIONS COMPANY
CB.....	CENTRAL BUDGET
CEFTA.....	CENTRAL EUROPEAN FREE TRADE ASSOCIATION
CITA.....	CORPORATE INCOME TAX ACT
CITUB.....	CONFEDERATION OF INDEPENDENT TRADE UNIONS IN BULGARIA
CoM.....	COUNCIL OF MINISTERS
CPC .....	COMMISSION FOR PROTECTION OF COMPETITION
EA.....	ENERGY ACT
EA.....	EXECUTIVE AGENCY
EAD .....	SOLE PROPRIETORSHIP JOINT STOCK COMPANY
EBRD.....	EUROPEAN BANK FOR RECONSTRUCTION AND DEVELOPMENT
EC.....	EUROPEAN COMMISSION
EC.....	EUROPEAN COMMUNITY
EDC .....	ELECTRICITY DISTRIBUTION COMPANY
EEEA.....	ENERGY AND ENERGY EFFICIENCY ACT
EU.....	EUROPEAN UNION
FDI.....	FOREIGN DIRECT INVESTMENTS
FDLG.....	FOUNDATION FOR DEVELOPMENT OF LOCAL SELF-GOVERNMENT
FR.....	FISCAL RESERVE
FSC .....	FINANCIAL SUPERVISION COMMISSION
FTA.....	FREE TRADE AGREEMENT
GDP.....	GROSS DOMESTIC PRODUCT
GS .....	GOVERNMENT SECURITIES
GVA .....	GROSS VALUE ADDED
HPP .....	HYDRO POWER PLANT
ICT.....	INFORMATION AND COMMUNICATION TECHNOLOGY
IMF .....	INTERNATIONAL MONETARY FUND
MAF .....	MINISTRY OF AGRICULTURE AND FORESTRY
MEER.....	MINISTRY OF ENERGY AND ENERGY RESOURCES
MLSP.....	MINISTRY OF LABOR AND SOCIAL POLICY
MoE .....	MINISTRY OF ECONOMY
MoF .....	MINISTRY OF FINANCE
MoH.....	MINISTRY OF HEALTH
MTC.....	MINISTRY OF TRANSPORT AND COMMUNICATIONS
NA.....	NATIONAL ASSEMBLY
NEC .....	NATIONAL ELECTRICITY COMPANY

## ABBREVIATIONS USED

NFA.....	NATIONAL FRAMEWORK AGREEMENT
NGO .....	NON-GOVERNMENT ORGANIZATION
NHIF .....	NATIONAL HEALTH INSURANCE FUND
NSI.....	NATIONAL STATISTICS INSTITUTE
NSSI .....	NATIONAL SOCIAL SECURITY INSTITUTE
OPF .....	OCCUPATIONAL PENSION FUND
PA.....	PRIVATIZATION AGENCY
PF .....	PENSION FUND
PIC.....	PENSION INSURANCE COMPANY
PIT .....	PERSONAL INCOME TAX
PITA.....	PERSONAL INCOME TAXATION ACT
PPA.....	PUBLIC PROCUREMENT ACT
RES .....	RENEWABLE ENERGY SOURCE
RIEW .....	REGIONAL INSPECTORATE OF THE ENVIRONMENT AND WATER
SERC.....	STATE ENERGY REGULATORY COMMISSION
SHEI .....	STATE HIGHER EDUCATION INSTITUTION
SME.....	SMALL AND MEDIUM-SIZED ENTERPRISES
SMEA.....	SMALL AND MEDIUM-SIZED ENTERPRISES ACT
SMPI.....	SUPPLEMENTARY MANDATORY PENSION INSURANCE
SSS .....	STATE SOCIAL SECURITY
TDP .....	TAX DEPRECIATION PLAN
TP .....	TAXABLE PERSON
UDB.....	UNION OF DENTISTS IN BULGARIA
UNDP .....	UNITED NATIONS DEVELOPMENT PROGRAM
UPF .....	UNIVERSAL PENSION FUND
USAID.....	UNITED STATES AGENCY FOR INTERNATIONAL DEVELOPMENT
VAT .....	VALUE ADDED TAX
VATA.....	VALUE ADDED TAX ACT
VPF.....	VOLUNTARY PENSION FUND
WB.....	WORLD BANK
WTO .....	WORLD TRADE ORGANIZATION

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*The positive assessment of Bulgaria's economy in the last quarter of 2003 is based on GDP's growth and on the good development of certain economic sectors. The quarterly results confirmed the positive trends for macro indicators such as inflation and unemployment level on an annual basis. In this quarter tourism, capital market and banking system data register improvement as well.*

*Overall the sector policy in the energy, environment and agriculture sectors can be given a positive assessment, whereas no serious developments were registered in the transport and in the high technologies and communications sector. Despite the steps towards improving the enterprise policy and the entrepreneurial environment, the Estat index of business climate in Bulgaria registered a negligible quarterly decline.*

A general **economic growth** of 4.3 per cent is projected for the fourth quarter of 2003. The industrial sector is expected to have the highest share in GDP production growth, whereas investments will be a major growth factor for GDP consumption. Against the corresponding period of 2002, the economic growth in the fourth quarter of 2003 is characterized by preserved higher growth rate of industrial production on an annual basis with parallel leading growth rates of industrial sales on the foreign market, high production activity in the construction sector, delayed growth in the services sector, leading growth rate of the import of investment goods, abrupt increase of the attracted share capital in the foreign direct investments inflow structure.

The relative **increase of consumer prices** in the fourth quarter of 2003 is 4.7 per cent against the fourth quarter of 2002, registering a rise compared to the corresponding change of consumer prices in the fourth quarter of 2002 (3.4 per cent). Like in the previous quarter, in the fourth quarter of 2003 the **unemployment** indicator registered the lowest levels of the number of unemployed against the corresponding quarters of the last five years.

In the fourth quarter of 2003 the **balance of payments** current account registered a negative value of -USD 828.9 m as a result of the sizable negative share of the trade balance (-USD 934.6 m). This is the highest current account quarterly deficit since 1991. The financial account balance is positive, registering an improvement on an annual basis (from USD 626.2 m for the fourth quarter of 2002 to USD 829.1 m for the fourth quarter of 2003). The positive contribution of the foreign direct investments inflow to Bulgaria is important in this respect (USD 328.8 m). The total quarterly balance of payments is positive (USD 364.1 m) and contributes to the growth of USD 337.5 m in BNB's foreign exchange reserves.

**Trade** is again exceptionally intensive, with imports growing faster than exports. The result is a huge negative balance

of over USD 1 b (export FOB – import CIF). Exports register stable growth rates, the European orientation is confirmed and exporters' positions are stabilized. The trade dynamics of the different commodity sections does not generate concerns. The higher import of raw materials and investment goods is associated with the intensified economy and the increased industrial production, whereas the higher import of consumer goods – with the improved access to loans and the legalization of some illegal imports. The inflow of foreign direct investments is mainly a result of attracted share capital – through the privatization of the DSK Bank and through other (non-privatization) transactions. The other capital item registers reflux of funds owing to the paid short-term loans.

In January 2004 the integrated value of the **Estat Index** of business climate registered a modest decrease, mainly as a result of the decline in the Investment Attitude component and the slightly lower managers' assessments of the quality of their internal resources. Despite the decline, the value of the Estat index remains positive within the neutral section of the scale. The economic environment for business development is still characterized as "neither favorable, nor unfavorable". The positive trend of improved business climate, observed since the beginning of 2003, is rather feebly marked. The opinion of the business about some business environment indicators registers improvement – most important among these is the higher confidence in the banking system. This fact is becoming a stable trend. The attitude towards the start up of new business, the administrative barriers and somewhat towards the government administration registers a positive change compared to the previous quarters. Signs of a positive change in the business' attitude towards the tax policy are also observed as a result of the amendments in the field approved at the end of 2003.

According to the latest survey, the basic problems of the Bulgarian companies are associated with the practical implementation of regulations, the absence of sufficiently active policy on the promotion of entrepreneurship and the use of high technologies in the business. Concerns about the absence of sufficient transparency in the competitions for public procurement awarding and implementation are also registered. The insufficient belief of entrepreneurs in the benefits of the harmonization of Bulgarian with European legislation also generates concern.

In the fourth quarter of 2003 the **entrepreneurial environment** registered an upward trend. A special Enterprise Policy Directorate was set up within the Ministry of Economy, the dialogue with business associations intensified. In October CoM approved a number of amendments to the SMEA, including a change in the definition of SMEs, which are expected to promote entrepreneurship. But the commitments undertaken in the negotiation process with the EU have not been systematized and adequately presented to entrepreneurs.



Positive changes were also registered in the **policy for promotion of investments in the economy**. The new principle of individual administrative servicing of investors with capital investments above BGN 100 m has already been applied for the project of the Turkish company Sisecam.

The **access** of enterprises **to financing** increased. New higher amounts were negotiated within EU's pre-accession funds. The loans extended to the business by the banking system registered sizeable increase and this loan expansion creates preconditions for accelerated economic growth in the period 2004 – 2005.

The new Act on the Restriction of Administrative Regulation and Administrative Control of Economic Activity took effect in December. It is unique in terms of its restrictive for the Bulgarian bureaucracy principles. Despite that, **the regulatory environment** remains unfavorable for the Bulgarian business, which is clearly manifested by the 2002-2003 Global Competitiveness Report results announced in October.

**Corruption** remains a popular practice for Bulgarian entrepreneurs. The high corruption practices level increases the costs of the business and enhances the shadow economy.

CPC's work registered improvement in the quarter under review. It is probably the changed operational principle (the sector principle was replaced by a functional one), as well as the personal changes, that allowed to intensify the Commission's work and to take important and decisive steps towards protection of the mechanisms of economic competition.

Despite some revival in the area of **privatization**, PA's program was fulfilled neither in terms of the number of enterprises envisaged for privatization, nor in terms of the revenues planned. According to the 2004 privatization plan PA should continue to sell at accelerated pace via the stock exchange. Despite that, only 8 per cent of the enterprises envisaged for privatization are in the final phase of their preparation for privatization.

According to data for the fourth quarter of 2003, overall good execution of the budget under the consolidated fiscal program is reported for 2003. According to data from the Ministry of Finance, as of 31 December 2003 **a surplus on the consolidated fiscal program** was registered for the first time since 1999. Revenues and aids by the end of December 2003 amount to BGN 14 072 m, little over 105 per cent of the total annual amount planned in the consolidated budget program. Overall, non-tax revenues register better execution against annual calculations compared to tax revenues. **Expenditures** for the period amount to a total of BGN 14 071 m, or 103 per cent of the annual amount of expenditures under Budget 2003. Expenditure items registering savings include social expenditures and scholarships, as well as interest on domestic and foreign loans. A sizeable overdraft is reported for capital expenditures and subsidies.

At the end of December 2003 **the fiscal reserve** amounts to BGN 3 848.8 m, registering a decrease of BGN 886.3 m compared to the previous months, with deposits in BNB amounting to BGN 3 280.1 m and foreign exchange assets amounting to BGN 2 289.3 m.

At the end of the fourth quarter of 2003 total **government and government-guaranteed debt** amounts to BGN 16 509.8 m at BNB central exchange rates for the lev at 31 December 2003. Total debt registers a decrease of BGN 684.9 m compared to the third quarter of 2003. At comparable data, the **debt/GDP ratio** has dropped from 48.7 per cent at the end of September to 47.8 per cent at the end of December 2003. Against the same period of 2002, total debt registers a decrease of BGN 1 670.2 m due to the US dollar devaluation against the Euro in the review period and the repayment of interest and principals.

According to data from the Ministry of Finance, at the end of December **foreign debt amounts** to EUR 7 295.4 m (against EUR 7 657.4 m at the end of the third quarter of 2003), with government debt amounting to EUR 6 903.1 m (against EUR 7 261.4 m at the end of June) and government-guaranteed debt amounting to EUR 392.3 m (against EUR 395.9 m at 30 September 2003). **Domestic debt** amounts to BGN 2 241.1 m. Compared to the end of the third quarter of the year total domestic debt registers an increase of BGN 22.9 m.

Anegligible increase in the **number of unemployed Bulgarians** was registered in the last quarter of 2003. Such increase is conditioned by the end of the seasonal employment period in the tourism and the agriculture sector. Yet it is not expected to have significant effect on total unemployment.

An important event in the fourth quarter was the Strategy for Employment in Bulgaria, 2004-2010 approved by the Council of Ministers. It is a document based on the objectives of the European Strategy for Employment – full employment, labor quality and productivity, and a labor market guaranteeing a high degree of inclusion.

The fourth quarter of 2003 signals of serious problems for the **incomes of Bulgarians** and is not an encouraging finale of the year. After the increase of real incomes (average monthly wage of the employed and monthly income per household member) registered in the previous three quarters, the last three months of the year all but stopped this trend.

Against this background, the planned increase of the electricity and heat prices and of the excise duty on fuels in 2004 will create preconditions for social tension, negligible expansion or stagnation of consumption and continuing lower standard of living for large groups of Bulgarians in the long run.

Intensified activity of government institutions in the area of **social assistance** and the policy on curbing poverty in Bulgaria



was registered in the last three months of 2003. These topics were obviously in the focus of attention in the period under review and in this case the question is rather about the logical end of a process, which has started earlier, and not about some campaign or a single effort. From now on the challenge will be to effectively implement a large number of strategic and programming documents and to complete them with new and modern forms of social services. The success of the government policy in this field will be dependable on the result-oriented work of all institutions and the media to overcome the reticence of the society, of employers in the first place, towards the abilities and skills of the disabled people.

Major legislative initiatives in the **social security** area include the 2004 State Social Security Budget approved in December and the draft law on the guaranteed claims of workers and employees in the event of employer's bankruptcy. Signing the Social Security Agreement with Serbia and Montenegro and the Administrative Agreement on its Implementation, as well as the Administrative Agreement on Implementation of the Social Security Treaty with Spain, Bulgaria made an important step towards higher coordination of the national social security system with the systems operational in the EU Member States and the candidate countries.

Further, 4 new ordinances of FSC on the activity of PICs and PIC-managed PFs, as well as on the interests of the insured persons in such PFs were promulgated at the end of 2003. A campaign for transfer of insured persons from one pension fund to another starts since 1 January 2004 but experts expect that not more than 5-10 per cent of the insured persons will take the initiative. Data about the supplementary pension insurance funds for the fourth quarter reveal that the number of insured persons and the available net assets in UPFs have registered the highest growth compared to OPFs and VPFs. As at end of 2003 PIC Doverie AD has managed to attract the highest total number of insured persons for the three types of funds, but in terms of the market share it is second after PIC Allianz Bulgaria. For about a year the net assets in pension funds have registered an increase of 49.71 and according to BASPIC projections they will reach BGN 685 m in 2004. The emerging trend of growing diversification of pension fund portfolios, which illustrates a more efficient management of pension assets, is given a positive assessment.

As regards **health policy**, NHIF, BDU and UDB declared willingness to have the 2004 National Framework Agreement signed on time and taking effect without delay, but unfortunately that did not come true. MoH did not present the four new ordinances regulating the basic implementation principles of the national health policy until end of December. There was also serious split of opinion between the doctors and the national health insurance fund on the new mechanisms to finance medical institutions proposed by NHIF and MoH. The Association of Private Medical Institutions proposed equal

treatment in the financing of state-owned, municipal and private medical institutions, but this approach is still regarded as radical and its implementation is not supported.

The first Bulgarian positive list of medicines, which protected the interests of the generic industry, caused the serious discontent of the Association of Research Pharmaceutical Producers and the Association of American Pharmaceutical Producers. The amount of the funds planned for medicines in NHIF's 2004 budget is by 45.3 per higher compared to the 2003 figure, but it is important to note that due to the absence of an integrated healthcare information system in the healthcare sector the funds for medicines may well prove insufficient again.

The passed Act on Blood, Blood Donation and Blood Transfusion introduced new measures for control on the quality and safety of blood and blood components. Another important legislative initiative in the last quarter of 2003 (the Supplemental Act to the Health Insurance Act passed by the National Assembly on 20 December 2003) solved the problems of persons who owe more than three health insurance payments for themselves and/or for members of their families for the period 2000 -31 December 2003. By the end of March 2004 they are to file with the regional offices of SSSI requests to be allowed to pay their obligations by installments till 31 December 2004.

In October 2003 Bulgaria ratified the Convention on the Access to Information about **Environmental** Issues, known as the Aarhus Convention. This act provides an opportunity to have an entirely new type of environmental policy implemented in the country. The fourth quarter of 2003 is also characterized by the steps the government administration took to project and program in a long-term perspective the management, processing and utilization of household and industrial waste whereby the relationship of the different actors in this process – government bodies and organizations, private subjects and citizens – are comprehensively regulated. The period is also characterized by the successful start of a couple of big environmental projects of Bulgarian companies for trade in noxious emissions within the opportunities provided by the Kyoto Protocol to UN's Framework Convention. The contracts within the Bulgaria-Austria Tzankov Kamuk Hydrosystem Project, the Biomass Utilization in Svilova AD – Svishtov Project implemented in cooperation with World Bank's Prototype Carbon Fund and the ERUPT Project for a gas-transfer network in the region of Veliko Turnovo implemented by Overgas Inc. and the Dutch Government were signed in the last months of the year.

Financial intermediation in Bulgaria continued to be effected mainly through the **banking system**. The credit expansion persists, but the condition of banks remains stable, with excellent indicators of capital adequacy and liquidity and well-functioning banking supervision. Nevertheless, receivables on loans to the non-government sector slackened their pace in the fourth

quarter. The banking system continued to increase its assets, deposits and current profit. But assets growth rate was lower compared to the previous quarter, whereas deposits growth rate increased against the previous quarter. The privatization in the banking sector was formally completed in the beginning of the quarter. After the sale of DSK Bank AD over 97 per cent of the total banking system assets are held by private persons and foreign banks and investors control more than 85 per cent of bank assets. The discussion about possible threats consistent with the intensified lending activity of the banks continued. IMF representatives were particularly insistent on the need of stricter control on the lending activity of banks. Despite the awareness of the benefits of intensified lending for the economic growth and the absence of immediate threats for the stability of the banking system, BNB accepted the arguments of IMF. The measures taken along these lines included in the first place an amendment of Ordinance No. 9 of BNB. The other events in the fourth quarter, which were significant for the operation of the banking system, included the approved new Ordinance No. 10 on the internal control in banks and the new General Conditions for cash servicing of BNB customers with banknotes and coins in the form of valuable parcels, effective since early November. The development of the privatization procedure for the national card operator Borica AD was another important event in the reviewed period.

The fourth quarter of 2003 was the end of a successful year for the Bulgarian **capital market**, despite that in this period the upward trends in some indicators were broken. Stock exchange trade remained active during the quarter, with turnover registering growth on the stock and bond markets, but some decline on the compensatory instrument markets. The SOFIX index increased to reach record high values, although it lost some of its value in the second half of the quarter. Market capitalization increased again during the quarter. Low liquidity remains a major problem irrespective of the positive trends in recent quarters. The number of issues registered for trading continues to be high but liquid positions are few (these are most of the securities included in the SOFIX index plus some of the former privatization funds). This quarter confirmed the impression from the recent year that market actors need and begin to follow carefully the fundamental factors influencing share prices (financial information and news from traded companies in particular). The price dynamics of shares, especially on liquid positions, increasingly reflects corporate events, which is a sign of better investment culture of market actors and improved market efficiency as a whole. In the last quarter of 2003 the shares of another open-ended investment company were accepted for trading on the stock exchange. In the fourth quarter FSC also issued one new open-ended investment company license. In October Bulgarian Stock Exchange – Sofia AD changed the list of issues used to calculate the SOFIX index. Issues are now 13 and not 10. The secondary trading in non-cash instruments of payment registered a decrease on a quarterly basis. As regards

capital market regulation, FSC approved a couple of entirely new ordinances (replacing previous analogous ones).

Two events of significant importance for the **energy sector** occurred in the past quarter. The Energy Act was finally passed almost at the same time with the official start of the privatisation of EDPs. The signed Memorandum of Understanding on the Southeast Europe regional energy market and its integration in EU's internal energy market was a step forward towards the establishment of a regional energy market. The building contract for the Tzankov Kamuk HPP and dam-lake, implemented within the Kyoto Protocol, was signed. International oil quotations registered an increase. The trend was accompanied by an increase of oil product excise duties in Bulgaria.

In the past quarter the **transport sector** did not witness any developments towards substantial progress in the sector's restructuring or evolution. The focus was placed on changing the sector's legislative framework and on the sale of Varna Dockyard. The State demonstrated willingness to allocate sizable resources to improve the transport infrastructure quality, but the realization of these intensions is rather questionable.

The last quarter of 2003 did not bring any significant changes in the **high technology and communications sector**. The good news was the first registration and public sale of shares in a technological company at the stock exchange. The Bulgarian e-Government topic was again in the focus of attention, but this time without any significant development or actions on the part of process actors. At the same time, the data by the national card operator Borica AD reveal again a serious growth in e-payments (via Internet, ATM or telephone). The preserved positive trends indicate quick penetration of information technologies in people's everyday life, which is a result of the improved technological literacy and the higher confidence in advanced technologies.

The positive trends in the development of **tourism** continued in the fourth quarter of 2003 - revenues from tourism reached USD 237 m, registering an increase of 29 per cent compared to the same period of 2002 when they amounted to USD 183.4 m. The winter tourist season had a successful start owing to the investments made in all winter resorts – Bansko in the first place, where a new cable car and new tracks were opened. A number of tourist sites were rehabilitated in Pamporovo and Borovez. Notable is the attempt of hoteliers and tourist companies to prolong the active tourist season through the promotion of congress and rehabilitation tourism, as well as other forms of tourism in the resorts.

The efforts made resulted in a growing number of foreign tourists with higher purchasing power in Bulgaria's winter resorts. Great Britain, Germany, Greece, etc. account for the highest number of tourists. Another positive trend is also observed – Russian tourists come back in Bulgaria's winter resorts. Amendments

to the Tourism Act were passed on first reading in the fourth quarter of 2003. Their main aim is to improve the environment for sector development. The plan is to set up a tourism executive agency, to facilitate the registration treatment in the tourism sector, to improve the categorization system for tourist sites, etc. A number of forums were organized to present the Bulgarian tourist product, of which the first regional conference on Biodiversity and Ecotourism in Southeast Europe is very important.

As regards **agriculture**, three important points concerning the further restructuring of the sector are worth noting. First, the census of operating farms was completed, which will provide opportunities to protect to the maximum Bulgaria's position in the negotiations with the EU on the financial framework and the quotas. Second, land consolidation projects were launched, which indicates the serious intentions of MAF and the donors to solve this problem, which is fundamental for the successful restructuring of the Bulgarian agricultural sector. Third, despite the violent debates on and the controversial assessments of the need and advisability of the government intervention on the grain market to limit the negative effects of the poor grain crop, the intervention eased the market and stabilized the price at a level corresponding to the international market conjuncture. This measure generated protests by the participants in the market, as preconditions for unfair competition were created and the market relationship was disturbed. The ambiguous intervention policy of the government, which was oriented towards solving problems "piece by piece" and imposing political/social reasons on the business, as well as the absence of long-term measures to overcome critical situations make the market unpredictable and impede normal market relations. This situation outlines the need to quickly establish and make operational an intervention agency similar to the one in place in the EU.

In the last quarter of 2003 the efforts to complete **the EU accession negotiations** on Chapter 24: Justice and Home Affairs resulted in temporary closing of this chapter. With the temporary closing of Chapter 24: Justice and Home Affairs, Bulgaria has completed the negotiations on total 26 negotiation chapters. Chapter 6: Competition Policy, Chapter 7: Agriculture, Chapter 21: Regional Policy and Chapter 29: Fiscal and Budgetary Issues remain open. The European Commission's Regular Report on Bulgaria's Progress towards Accession was published in November. Bulgaria's macroeconomic stability was given good assessment. The recommendations for Bulgaria in the regular report concern the flexibility of markets and the need of further structural reforms, including the administration and the judiciary system.

The local elections of mayors and municipal councilors at the end of October were the most important event in the fourth quarter of 2003, which has incontrovertible effect on **regional development**. The new local government representatives declared their readiness to follow the continuity principle in

local government, which gets increasingly established as an important element of Bulgaria's democratic development. The preparation of the Bulgarian municipalities for Bulgaria's accession to the EU in 2007 was declared a major priority in the work of local authorities.

Legislative efforts were focused on distinguishing the powers and cooperation of local and central authorities, on clearly defining the rights and responsibilities of local authorities within their terms of reference, on the financial and property independence of municipalities through increased tax powers and higher independence in the draw up and management of municipal budgets. A specific step along these lines is the started implementation of the decision to have the municipalities collect alone the local taxes and charges. But some experts are afraid that many municipalities are not prepared to collect alone the local taxes and charges – they might encounter problems in calculating the charges and taxes, hence the need of adequate training. The implementation of projects resulting in improved quality of municipal services for the business and the people continued in the fourth quarter. New instruments of European programs were also announced – the External Borders Initiative within the PHARE Program to be implemented since 2004. The objective of this initiative is to improve the standard of living in border regions, to develop trans-border cooperation and to support the activity in the economy, culture, tourism, and environment sectors. The initiative covers Bulgaria, Serbia and Montenegro, FYR Macedonia and Turkey.

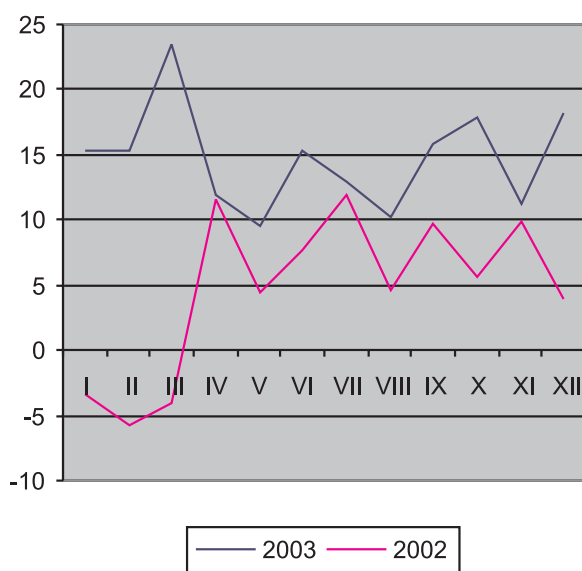
## Gross Domestic Product

**Economic growth in the fourth quarter** of 2003 could exceed the 3.4 per cent growth in the same period of last year and reach 4 per cent, mainly due to production growth in the industrial sector and investment growth in terms of GDP use.

**NSI monthly business surveys** for October - December 2003 outline a slightly improved economic climate compared with the corresponding quarters of the previous two years, when business climate levels tended downward. It is noteworthy that in October 2003 the general business climate indicator rose considerably on September (by 1.8 percentage points), in November dropped by 3.8 percentage points on October and in December rose again - by 1.8 percentage points on November - as a result of the more favorable economic situation in industry and construction.

Compared with the same period of 2002, economic growth in the fourth quarter of 2003 was characterized by sustained higher **industrial production** growth on an annual basis, combined with faster growth in **industrial sales**.

Figure 1. Industrial production growth rate, corresponding month of the previous year =100, %

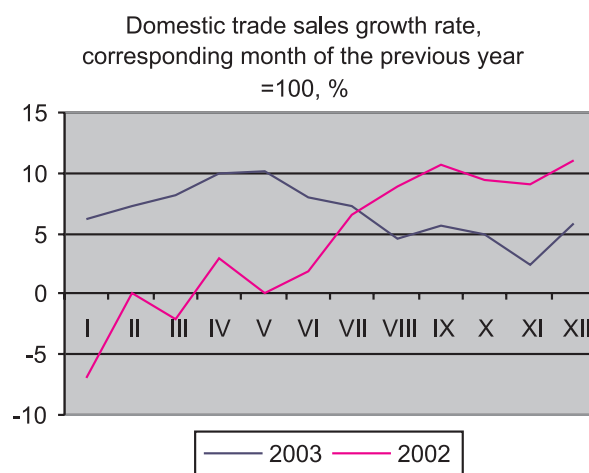


Source: NSI.

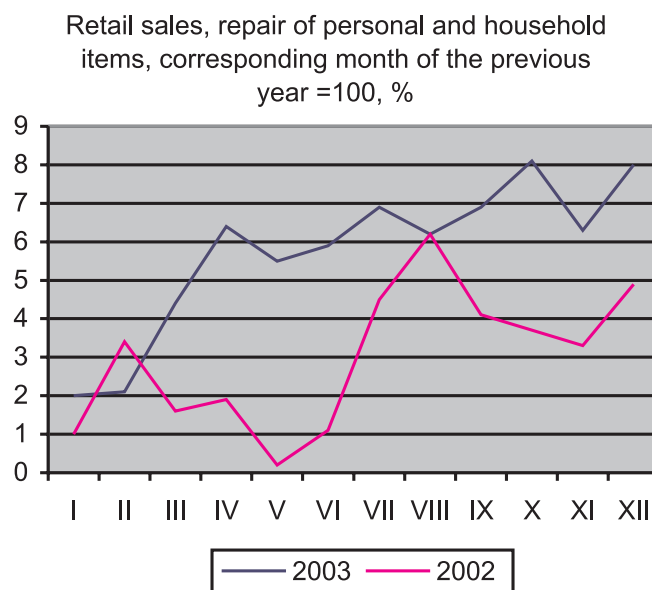
The positive dynamics in industrial production accelerated on an annual basis in the fourth quarter. Higher growth rates were achieved both in comparison with the corresponding period of 2002 and the third quarter of 2003. This is confirmed by the data from the NSI business surveys, which estimate the current production activity in industry as upward, unlike the downward trend in the same period last year. Therefore we could assume higher value added growth in industry compared with the fourth quarter of last year. A major factor for growth in industry in the fourth quarter and the whole 2003 is external demand – export sales grew by over 30 per cent on an annual basis, or over 4

times faster than domestic market sales. It should be noted that business climate in construction registered considerably higher levels in the fourth quarter of 2003 compared with previous years. This gives ground to expect that growth in construction will probably exceed growth in the fourth quarter of last year. Therefore we expect **value added growth in the industrial sector** as a whole will exceed considerably the 3.1 per cent growth in the fourth quarter of 2002.

Figure 2. Trade sales growth rate



Source: NSI.



Source: NSI.

In the fourth quarter of 2003 slowdown in **services sector** growth continued. Growth in **domestic trade sales** slowed further, although **retail sales** continued growing at a faster pace compared with the fourth quarter of 2002. NSI business surveys in trade also showed that business climate in retail trade in the fourth quarter of 2003 is more unfavorable compared with the corresponding period of last year. Compared with the fourth quarter of 2002, business climate in the other services, captured as a separate sector by the NSI business surveys, is



more unfavorable in the fourth quarter of 2003. We expect that value added growth in the services sector as a whole will not exceed growth in the past year's fourth quarter. On the other hand, we assume a considerably higher growth in industry. **The growth could not only compensate the prevailing weight of the services sector in the structure of GDP produced but will also contribute to a higher overall economic growth (about 4.3 per cent) compared with growth in the fourth quarter of 2002 (3.4 per cent).**

Typical for the whole 2003 is that value added in industry grew at much faster pace than value added in services, in contrast to 2002. In the third quarter of 2003 value added in industry rose by 8.4 per cent on an annual basis, while value added in services grew by 4.2 per cent, industry and services contributing to GDP growth by 2 percentage points each. Should there be no revision of GDP growth data in the first three quarters of 2003 and assuming a fourth quarter growth of 4.3 per cent, **our estimate for the overall economic growth for 2003 as a whole is at some 4.2 per cent.**

Our expectations for economic growth in gross domestic product used are based mainly on the expectations for higher growth in investments, compared with the fourth quarter of 2002.

The slowdown in **growth of households' incomes** since August 2003 compared with their growth in the corresponding months of 2002 continued in the fourth quarter of 2003 – on an annual basis average real income per person from a household grew at less than 4 per cent against 16 per cent in the same period of 2002. On the one hand, growth in income from salaries on an annual basis is negligible – below 0.1 per cent against 2.5 per cent real growth in average monthly salary of employees in the fourth quarter of 2002. On the other hand, transfers from individuals continued (in the fourth quarter of 2003 these amounted to USD 191.8 million against USD 153.1 million in the same period of 2002). Growth in retail sales continued growing faster. In addition, although monthly growth in credits to households slowed, at the end of the year these increased by 77 per cent on December 2002.

We expect **investment in fixed assets** in the fourth quarter of 2003 will have a two-digit growth rate on an annual basis. Although in the fourth quarter wholesale sales grew more slowly than in the corresponding period of 2002 and the annual growth in credits to private non-financial enterprises stood at 41 per cent at the end of the year, imports of investment goods grew in nominal dollar terms by 36 per cent – almost twice as faster compared with their growth in the fourth quarter of last year (19 per cent). It is important to note that in the fourth quarter of 2003 the structure of **foreign direct investment** inflow changed dramatically, reflecting an increase in borrowed share capital, while in the previous quarters of 2003 investment in other capital made up the largest share. On an annual basis

the nominal lev equivalent of foreign direct investment inflow in the participation in the capital item doubled against a mere 7 per cent nominal growth in the corresponding quarter of 2002. Although imports of goods and services continued growing faster in nominal terms than exports of goods and services, in the fourth quarter of 2003 the negative effect on overall economic growth was not as severe as it was in the previous two quarters, and the nominal lev growth of imports and exports of goods and services is 8.8 per cent and 6.1 per cent on an annual basis against 12.3 and 7.7 per cent in the fourth quarter of 2002. In the fourth quarter of 2003 import prices continued falling while export prices continued growing.

## Inflation

In the third quarter of 2003 **business surveys and users survey of NSI signaled higher inflationary expectations.** In the fourth quarter of 2003 the relatively smooth price dynamics was disturbed by the increased consumer prices of several groups of foodstuffs (bread, meat, fresh vegetables) in November and December, which contributed to twice as high monthly inflation to 1.8 per cent and reflected on a **5.6 per cent cumulative inflation at the end of the year against December 2002.** The relative increase in consumer prices in the fourth quarter of 2003 against the fourth quarter of 2002 is 4.7 per cent, exceeding the corresponding change in consumer prices for the fourth quarter of 2002 (3.4 per cent), but thinner and smoother price dynamics since the beginning of 2003 compared with 2002 resulted in **lower average annual inflation for 2003 (2.3 against 5.8 per cent for 2002).**

**Industrial producer prices** on the domestic market continued increasing gradually within the range of below 1 per cent monthly and in the fourth quarter of 2003, exceeding their December 2002 level by 4.2 per cent at the end of the year.

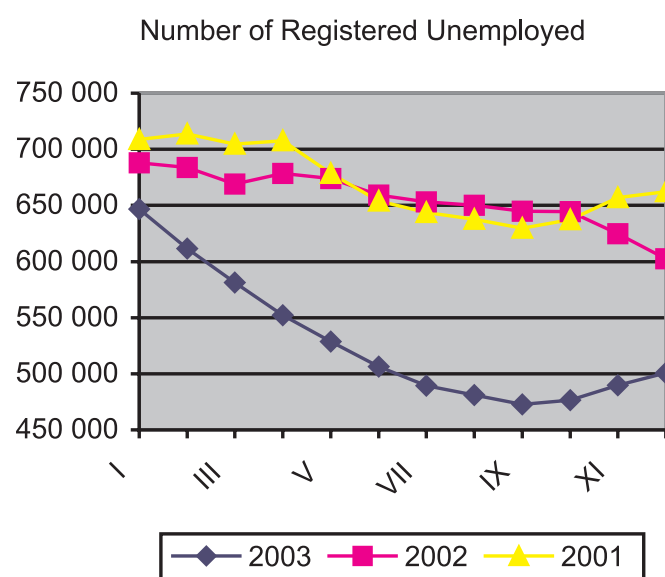
## Employment and unemployment

**At the end of 2003 registered unemployed numbered 500 664 and the unemployment level was 13.52 per cent.** Increased unemployment at year-end is a typically seasonal phenomenon for the period beginning 1991. However, **the downward trend in unemployment could be determined as sustainable – the number of unemployed decreased by over 100 000 or 17 per cent on December 2002, the biggest December-on-December decline in absolute and relative terms over the past three years.** Of note is the fact that, similarly to the third quarter, monthly unemployment levels in the fourth quarter hit a record low compared with the same quarters of the past 5 years.

**A trend toward improvement of the position of young people on the labor market** has started – in the fourth quarter of 2003 the share of employed young persons of up to 29 years

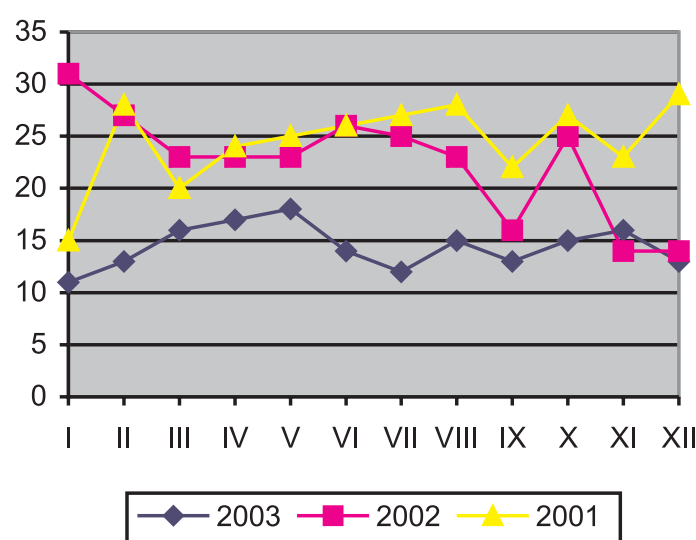
of age continued increasing from September and reached 35.5 per cent in December. Throughout 2003 the levels of registered unemployed per one job reported at the Employment Agency stood continuously low.

Figure 3. Number of registered unemployed



Source: EA

Number of registered unemployed per one job



Source: EA

## Balance of Payments

The current account ran a deficit of USD -828.9 m in the fourth quarter, the biggest absolute figure for all quarterly current account deficits since 1991. The deficit is accounted for by the significant negative contribution of the trade balance (USD -934.6 m) and the balance on services (USD -111.2 m), combined with a modest positive contribution of the balance on

current transfers (USD 193.8 m) and the balance on income (USD 23.0 m).

The current account deficit worsened by USD 194.4 m on the same period of 2002.

The worsened trade deficit (FOB/FOB) by USD 225.2 m on the same period of 2002 exceeds the absolute value of the change in the current account by over 16 per cent. In the fourth quarter the worsening of the balance on services on an annual basis (by USD 55.7 m) represents 28.7 per cent of the absolute value of the change in the current account. The balances on income and current transfers improved by USD 61.2 m and USD 25.3 m, offsetting the worsening of the current account deficit and accounting for 31.5 and 13.0 per cent of the absolute value of the change in the current account.

Table 1. Change and contribution to the current account change in 2003 on the corresponding period of 2002 and in 2002 on the corresponding period of 2001

	Q1 2003	Q2 2003	Q3 2003	Q4 2003	2003
million USD					
Current account	-170.2	-435.6	-135.2	-194.4	-935.5
Trade balance	-58.1	-301.1	-294.8	-225.2	-879.3
Services (net)	-55.3	0.1	91.7	-55.7	-19.2
Income (net)	-105.2	-138.6	5.4	61.2	-177.3
Current transfers (net)	48.6	4.0	62.4	25.3	140.3
Current account = 100, %					
Current account	100.0	100.0	100.0	100.0	100.0
Trade balance	34.1	69.1	218.0	115.8	94.0
Services (net)	32.5	0.0	-67.8	28.7	2.1
Income (net)	61.8	31.8	-4.0	-31.5	19.0
Current transfers (net)	-28.6	-0.9	-46.2	-13.0	-15.0
	Q1 2002	Q2 2002	Q3 2002	Q4 2002	2002
Million USD					
Current account	-23.6	12.8	359.8	-219.4	129.6
Trade balance	-28.5	39.9	168.8	-194.2	-14
Services (net)	-39.6	11.3	100.2	-22.1	49.8
Income (net)	52.3	-29.4	44.1	-24.4	42.6
Current transfers (net)	-8.0	-9.1	46.8	21.3	51
Current account = 100, %					
Current account	100.0	100.0	100.0	100.0	100.0
Trade balance	120.8	311.7	46.9	88.5	-10.8
Services (net)	167.8	88.3	27.8	10.1	38.4
Income (net)	-221.6	-229.7	12.3	11.1	32.9
Current transfers (net)	33.9	-71.1	13.0	-9.7	39.4

Source: BNB and own calculations.

The balance on the financial account was positive and improved on an annual basis (from USD 626.2 m in the fourth quarter of 2002 to USD 829.1 m in the fourth quarter of 2003).

It is accounted for mainly by the positive contribution of direct investment inflow into Bulgaria (USD 328.8 m), a decrease in other investment – assets (USD 204.1 m) and the increase in other investment – liabilities (USD 327.8 m).

Within the elements of the other investment – liabilities item external credits to “other sectors” (private nonfinancial sector) increased by USD 75.6 m in the fourth quarter of 2003, exceeding considerably the increase in the corresponding period of 2002, combined with an increase in nonresidents’ deposits by USD 158.3 m, a sharp increase compared with the other quarters of 2003 and tripling the increase in the corresponding quarter of 2002.

The overall balance of payments for the quarter was positive, amounting to USD 364.1 m, and together with the decreased net liabilities to the IMF by USD 26.6 m led to a USD 337.5 m growth in BNB forex reserves.

**For the 2003 as a whole the deficit on the current account of USD 1648 m (8.7 per cent of GDP) more than doubled the deficit for 2002 (USD 712.6 m or 4.6 per cent of GDP respectively).** The worsening of the trade balance (94.0 per cent) was the main factor responsible for the current account worsening in 2003. Worsened trade balance in 2003 is consistent with the faster growth in imports, mainly driven by domestic credit growth. The negative contribution of the Income (net) item for the worsening of the current account (19 per cent) was realized in the first half of the year, mainly reflecting a growing debt to the private sector, the operations on government debt restructuring and dividend payments. The overall annual contribution of services on the change in the current account was negative (2.7 per cent of the annual worsening), while improvement of the Current transfers (net) item contributed by 15 per cent to offset the negative effect of the trade balance and the net income.

Growth in BNB forex reserves at the end of the year helped improve the BNB forex reserves/Imports of goods and nonfactor services ratio (6.5 months) on December 2002 (6.1 months).

## Foreign trade

**The trade balance deficit for the first time exceeded USD 1 billion (exports FOB - imports CIF) and grew by 30 per cent on the fourth quarter of 2002.** The reason for this is the ongoing faster growth in imports (28 per cent) than exports (26.4 per cent). Despite the impressive data it cannot be said that something extraordinary had happened. A year ago (the fourth quarter of 2002) the difference in growth rates was much more significant and the deficit increased faster.

Changes in the **commodity structure of exports** in the fourth quarter of 2003 compared with the same period of 2002 are associated with the increased share of consumer goods (from

34.9 to 37.4 per cent) at the expense of the share of energy resources (8.4 and 5.9 respectively). Raw material feedstocks and investment goods sustained their levels, their exports increasing at rates close to total exports levels. Machines and appliances (35 per cent) and spare parts accounted for the main share in investment goods. Ferrous and nonferrous metals evolved into competitive exports, registering some 40 per cent growth on the fourth quarter of 2002. Even in chemicals and fertilizers, which are no longer structurally significant for Bulgarian exports, growth is impressive – more than double in fertilizers and over 30 per cent in chemicals. The condition of the Bulgarian textile industry is reflected in the fact that exports of textiles and clothing grew at close rates (about 40 per cent) and their share in total exports rose from some 23 per cent to 25.3 per cent. As regards the food sector, exports of raw material feedstocks for production of foodstuffs halved at the expense of higher exports of finished foodstuffs (by more than 44 per cent).

No significant changes evolved in the **geographic structure of exports**. Exports to EU grew faster than total exports and their share reached 56.8 per cent. Italy preserved its leading position among the countries consuming Bulgarian export products, but Germany and Greece are almost catching up with it as exports to those two countries grew by 51 and 62 per cent respectively for one year. Turkey retained its fourth place but its share in total Bulgarian exports fell from 9.1 per cent in the fourth quarter of 2002 to 7.8 per cent a year later. Exports to Balkan countries increased, accounting for 7.5 per cent of total exports (against 7 per cent a year earlier).

**Imports by major commodity sections** – consumer goods, raw material feedstocks and investment goods – grew at similar rates, while the share of energy resources decreased in absolute and relative terms. Imports of furniture and household items increased most significantly (more than 50 per cent), probably associated with the banks’ credit expansion and easier access to consumer credits. Increased imports of raw material feedstocks and investment goods (by 36 per cent) are consistent with economic turnaround and higher industrial output.

**Half of imports in the fourth quarter came from the EU** (against 47.6 per cent a year earlier). This is due to the faster growth in imports from those countries, compared with total imports growth. A similar development occurred in trade with CEFTA countries, which already account for 9 per cent of total imports. Imports from Turkey and Greece grew most significantly probably due to tightening of the customs regime and bringing into “light” some of the illegal flows. Germany, Italy and Greece remain the biggest suppliers of import goods to the Bulgarian market, followed by Russia (second place) and Turkey. Those five countries account for more than half of imports to Bulgaria.



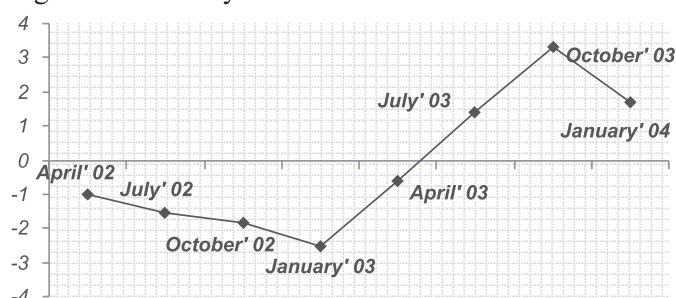
### Foreign direct investments

Higher trade deficit is directly related to foreign investment inflow, which continued growing to reach USD 1.361 billion for 2003 as a whole. The USD 328.8 billion invested in the fourth quarter represents a 22.5 per cent increase on a year earlier. Unlike previous periods when attracted funds under the Other capital item had increased, representing mainly credits from investors to companies with foreign stake, now investments are entirely in share capital – from privatization (e.g. DSK Bank) and from other non-privatization deals. Preliminary data about the fourth quarter show an outflow of funds under the Other capital item due to repayment of short-term credits. Data about reinvested profits are not available yet. Practice shows that the announced value of foreign direct investment inflow increases considerably in subsequent revisions. **This gives us ground to expect that actual investments for the year will approximate USD 2 billion.** For the time being it is clear that in 2003 investment dynamics accelerated resulting in total foreign direct investment growth of over 50 per cent.

## The Estat index of business climate in Bulgaria

The integrated value of the **Estat index of business climate** in January 2004 fell to **+1.67** from +3.33 in October 2003 (Figure 4). The main reason is the fall in the "Investment attitudes" component and less favorable managers' assessments of the quality of resources of the companies managed by them. Despite the fall, the **Estat index** remains positive in the neutral part of the scale. The economic environment for business development again is characterized as **"neither favorable, nor unfavorable."**

Figure 4. Dynamics of business climate condition



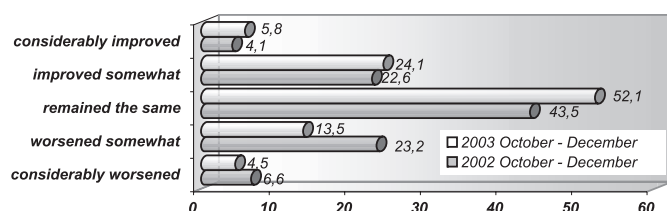
## General condition of the business sector

The value of Component I "General condition of the company" fell from 8.69 in October to **7.78** in January 2004.

The study shows that as a whole the positive trend evolving in 2003 toward improving the condition of the business sector is slightly pronounced.

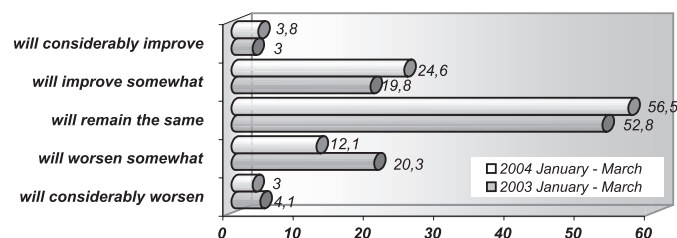
According to 30 per cent of the managers (Figure 5), in the last quarter of 2003 the business of the companies managed by them improved, a slight fall on July – September 2003 period. Possible reasons for this are observed seasonal fluctuations in assessing the condition of economic subjects. The comparative analysis of the data from all studies shows a certain increase in the share of managers' negative assessments and skepticism in the winter months of the year. The share of companies experiencing difficulties in their business has changed more significantly.

Figure 5. In your opinion, has the condition of your business changed? (by quarters)



Assessment of growth prospects is rather moderate compared with the previous study. Reserved short-term forecasts about this indicator prevail (Figure 6).

Figure 6. Will the condition of your business change in the months January – March 2004?



The share of companies not having competitive advantages continued to increase, though slightly (Table 2). We registered a slight decrease in the share of companies with 3 and more advantages. The main reasons could be sought in managers' lower assessments (compared with the previous study) of core business resources. Companies' difficulties are mainly related to the low quality of financial resources and 10 per cent state they do not have any. The share of enterprises without computers and software, information input and Internet decreased. The study showed a sustainable trend in this respect throughout the two-year period since the launch of the **Estat index**. Already three out of four Bulgarian companies use computers and Internet in their work.

Table 2. Companies position compared to competitors, %

Number of competitive advantages	2002			2003				2004
	April	July	October	January	April	July	October	January
none	19.5	28.3	32.5	33.1	27.1	28.5	30.8	31.6
1	19.8	13.1	16.3	17.0	16.6	16.0	17.1	15.3
2	18.8	24.2	17.6	18.3	22.1	17.9	16.4	19.3
3	16.5	14.4	13.9	12.0	11.6	10.8	11.6	15.3
4	13.2	7.8	10.8	10.3	9.5	11.5	11.6	8.3
5	7.1	6.9	3.7	4.0	6.0	7.9	5.0	5.0
6	5.1	5.3	5.2	5.3	7.0	7.4	7.3	5.3

## Assessment of investment attitudes

The component "Investment attitudes" decreased from 32.60 in October 2003 to **29.20** in January and contributed most significantly to the downward trend in the integrated **Estat index**.

The decrease is due to the lower share of those who agree with the following statements: "I would introduce new technology if

<sup>1</sup> The study was conducted in the period 20th - 29th January 2004 among managers of 409 companies and is representative at the level of going concerns. Criteria for selection of the companies in the sample are the region, sector, number of employed and type of ownership. The index methodology and the mathematical model are developed by the **ESTAT Agency for Market and Social Studies**.

this would enhance the quality of my products, regardless of whether this would have an impact on my profit” – from 81.2 per cent in October 2003 to 77.7 per cent in January 2004; “It is easy to find the employees I need” – from 51.2 per cent in October to 43.8 per cent in January, and “If I have excessive funds, I would invest them in another activity, even if there is a risk” – from 53 per cent in October to 48.2 per cent in January.

Managers focus their efforts on developing the core activity in the conditions of growing competition and taking into account the prospects for Bulgaria’s accession to the EU.

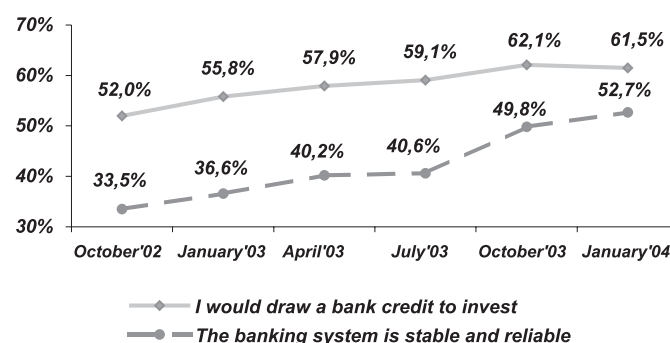
We observe a sustainable upward trend in the share of companies following a long-term development strategy. The percentage of managers who bind their business with strategic partners increased. The striving to develop the core activity is associated with overall mobilization of financial resources and thereby the share of managers stating deficiency of financial resources for business development remained high (Table 3).

Table 3. Investment attitudes and corporate strategies, %

Statements about investment attitudes and corporate strategies	Share of affirmative answers	
	2003	2004
	January	January
If I do not have funds for investment in core activity I will do my best to ensure them	83.0	88.4
I have a business strategy updated regularly	67.4	76.4
In my current activity I experience deficiency of financial resources	69.9	72.0
I have partners on which my business depends in the long run	46.3	57.6

A natural and the only available alternative at the moment to reduce companies’ deficiency of funds is bank lending. The share of enterprises that would draw a credit to implement their investment strategy remained high. The strongly pronounced positive trend in the attitude toward the banking system, evolving since late 2002, continued. The study measures it through two indicators – indirect, aptitude to taking bank credit, and direct, assessment based on stability and reliability characteristics. The figure below shows enhanced confidence in the banking system and perception of lending institutions as a real and main opportunity for business development (Figure 7). The reasons for the evolving positive attitudes could be sought mainly in the pro-active lending behavior of financial institutions, the increased number of credit facilities and the growing popularity of these services. In addition, a real fall in interest on credits is in place, in line with the short-term downward trend in interest globally.

Figure 7. Confidence in the banking system (share of those who agree with the statements)



In January the share of entrepreneurs (68 per cent) who consider the Bulgarian market as a priority in selling the products and services of the companies managed by them remained high. There is a direct relationship between the high aptitude to introducing new production technologies (78 per cent of the companies) and the drive for enhancing quality at any stage of the production process (97 per cent of the companies). Managers see a certain threat to the implementation of this strategy in the greater difficulty in finding qualified personnel. The share of managers who face such problems is 56 per cent. This is the highest registered value of the indicator since the start of the study.

## Assessment of the business environment

The value of this component of the **Estat index** remained unchanged.

As a whole, at the beginning of the year the representatives of the business were more optimistic about the business environment, compared with the previous year. Their opinion about most of the indicators characterizing the business environment has improved.

Firstly, these are the indicators assessing the start-up of new business and the role of administrative barriers. The business assessment of the start-up of new business is more positive in January 2004 – according to 14 per cent start-up of new business in the country is not a problem, while in October 2003 only 10 per cent of the respondents had that opinion. This is the highest value of the indicator since the beginning of conducting the business surveys in 2002. The change regarding the impact of administrative barriers is positive – 27 per cent of the respondents believe these are not a major problem for business, while in October 2003 20 per cent of the respondents had that opinion. It should be noted that this indicator is most favorable since the start of conducting the surveys. Probably the business opinion is influenced by the measures taken to reduce regulatory regimes. Moreover, at the end of the year the new Reduction of Administrative Regulation and Administrative Control on Economic Activity Act came into force. Although

its effect is not immediate – it is extended over time – the expectations of the representatives of the business are that it will lead to actual reduction of the administrative interference of the state in the economy.

Another positive noteworthy fact is the attitude toward government administration. In January the share of those who would pay additional money to avoid difficulties with the administration hit a record low, 77 per cent, while in October 2003 it was 84 per cent.

Table 4. Administration and administrative procedures, %  
(share of those who agree with the statements)

Statements about administration and administrative procedures	2003		2004
	January	October	January
Administrative obstacles are a major problem to business	77.5	80.3	73.0
Most businessmen would pay additional money to avoid difficulties with the administration	80.7	84.2	77.5

A positive change occurred in the opinion about the indicator assessing regulation of market competition compared with the previous survey and with the whole past year. The share of those who assess negatively the rules for competition protection fell from 86 to 81 per cent. A possible explanation for this is the fact that in October a new management team of the Commission for Protection of Competition was elected, expected to boost the activity of the Commission as an efficient anti-monopoly and regulatory body in this area.

Business opinion about the tax environment continued to improve. It is noteworthy that attitude to the patent tax as unbearable to the companies shows the lowest value since the start of the study – 41 per cent of the respondents define it as such while in the beginning of the business surveys 57 per cent of the respondents had that opinion, and in October 2003 51 per cent, respectively. A positive change occurred with regard to tax rates – 80 per cent of the companies had an absolutely negative attitude to them at the beginning of the study, while currently 72 per cent consider them high and a reason for income concealment. The profit tax is assessed as bearable by 29 per cent of the respondents while in the latest survey 23 per cent assessed it as such. Assessment of the tax system, as noted in the previous reports, shows a trend toward improvement – probably associated with the desire to introduce greater predictability and clarity as well as with the amendments to the Corporate Income Tax Act adopted at the end of last year and the changes in the patent tax rates. The change in the managers' assessment is based on the understanding that they could use the freed financial resources for reinvestment and modernization.

Table 5. Tax system  
(share of those who agree with the statements, %)

Statements about the tax system and legislation	2003		2004
	January	October	January
The tax system creates equal conditions for all companies in the country	15.3	13.7	12.7
Tax rates force companies to conceal incomes	71.8	79.5	72.6
The patent tax is unbearable to companies	50.5	51.7	41.5

The positive trend in business assessments of the stability and reliability of the banking system sustained – more than half of the respondents assess it as such, 52 per cent.

Although government policy in support of the business is generally assessed as negative, assessment of the legislative initiative of the government improved – already 15 per cent of the respondents define it as consistent and non-contradictory, against 10 per cent in October 2003. According to business representatives, major difficulties stem from the lack of efficient implementation of the legal framework – 76 per cent consider it as a problem and the share of those having such an opinion has increased (73 per cent in October 2003). This confirms the opinion that laws are being successfully harmonized with the European ones but their enforcement is a major weakness.

Transparency of public procurement bidding under the Public Procurement Act still causes concern among business representatives. In January support of the statement that the biddings are transparent and fair dropped to 7 per cent, its lowest value for the whole period of the study. The share of those who believe that the government pursues a policy of promoting research and use of advanced technologies decreased – in October 2003 it was 15 per cent against 11 per cent now.

The lower share of managers who believe that harmonization of Bulgarian legislation leads to improved business conditions causes concern. Assessments vary within a wide range, which suggests a lack of sufficiently consistent explanatory campaign and information about the benefits and difficulties regarding accession to the EU.

## Summary

The positive trend of early 2003 toward improving the condition of the business sector is rather weak. A possible reason for the reduction of the **Estat index** for the last quarter are the seasonal fluctuations in the assessments of the condition of business entities.

Confidence in the banking system and managers' aptitude toward using credits for business expansion increased. Bank lending has no alternative for the Bulgarian companies against the background of poor quality and even lack of own financial

resources. Compared with the previous quarter, criticism over the problems with starting up a new business, administrative barriers and government administration to some extent decreased slightly. There are signals of a positive change in the business attitude toward tax rates as a result of the adopted changes in late 2003.

According to the latest survey, the main difficulties faced by the Bulgarian companies are associated with the practical enforcement of the legal framework and the lack of sufficiently active policy of promoting entrepreneurship and using hi-tech in business.

According to the **NSI business surveys** business climate in the country improved slightly in the last quarter of 2003, compared with the corresponding quarters of the previous two years, when business climate levels had subsided till December. The main reason for this is the more favorable business climate in industry and construction.



In the fourth quarter **some positive trends** outlined in the elements of the business environment in Bulgaria:

- the institutional framework for entrepreneurship development improved;
- companies' access to financing expanded;
- some good practices in the regulatory and administrative environment were introduced;
- a number of projects in support of enterprises started;
- some industries began introducing European standards;
- the activity of the Commission for Protection of Competition, responsible for efficient operation of markets, improved;
- the privatization process stirred to some extent compared with previous periods.

However, some **negative elements** in the business environment and enterprise policy emerged:

- the government lags behind in acquainting the business with the requirements related to the future membership in EU;
- the expected dramatic improvement of administrative service is postponed so far;
- expenses of the business in communication with the administration increased;
- proposed positive changes in the legal framework on encouraging investment in the economy were delayed;
- the indicators envisaged in the privatization program were not achieved.

## Encouragement of entrepreneurship

Serious structural changes occurred at the Ministry of Economy aimed to turn it into a real subject of government economic policy and enterprise policy. With **the new Structural Regulation of the Ministry of Economy**, adopted in October, new directorates were created, directly responsible for general economic policy, enterprise policy, corporate management and restructuring, and investment policy. European Integration Directorate was retained, which will deal with the impact on the economy and enterprises' activity from applying the European legislation.

In October the CM approved **amendments to the Small and Medium-Sized Enterprises Act**, adopted at first reading by the National Assembly in January 2004. For the first time a clear distinction was made between the role and functions of individual government bodies in formulating, coordinating, controlling and implementing government policy of encouraging entrepreneurship. Thus the Ministry of Economy will formulate, coordinate and control government policy in support of the SME sector and the future Agency for Encouragement of Entrepreneurship (AEE) will be responsible for the implementation of the *national strategies and working programs for entrepreneurship encouragement*, adopted by the Council of Ministers.

**The SME Agency and the Agency for Trade Encouragement merged to form the new AEE.** This is in line with the need for export orientation of enterprise activity in the conditions of economic integration to the EU and economic globalisation.

**Regional branches of the new AEE** are being established, aimed to shorten the distance between entrepreneurs and the state, cut expenses for business start-up and operation, increase possibilities for higher quality consultation and better protection of their interests. Most of the new structures of AEE will be established on the basis of public-private cooperation between the state and the representatives of local business and business associations.

A positive feature of the draft law is that it **encourages participation of NGOs**, professional chambers and unions, associations supporting small and medium-sized enterprises and scientists in developing and implementing the policy of entrepreneurship promotion.

In addition, the new draft law changed the **definition of SME**, which provoked a number of discussions in the review period. According to the new definition, a micro company has personnel of less than 10 persons; small companies have personnel of 10 to 50 persons, with annual turnover of BGN 13 m and balance sheet value of the assets of up to BGN 9 m; medium-sized companies have personnel of 50 to 250 persons, with annual turnover of up to BGN 78 m and balance sheet value of the assets of up to 52 m. Overall, it is expected that the change in the definition will have a positive effect on entrepreneurship. This is due to several reasons: first, more enterprises will be able to apply for financing under European programs; second, the new definition allows **comparability between enterprise policies** in different countries (both candidates for membership and EU member states) because the **object of economic measures** in different countries will be the same; third, analyses of the sector of SME will also be **internationally comparable**; and fourth, the definition **harmonizes legislation** with the EU one, which is a step forward toward implementation of EU *acquis communautaire* in Bulgaria.

Amendments to this Act should not be viewed as a separate element from the other changes in the legal framework, to be made in the first quarter of 2004. They represent the first step toward providing government support to SME in their life cycle (start-up, development and export orientation). The next steps are adoption of the Encouragement of Investments in SME Act and amendments to the Foreign Investment Act, as well as implementation of the promulgated Encouragement of Scientific Research Act (which will promote knowledge transfer to SME, respectively higher degree of value added in their products).

## Encouragement of investments

Commitments to changing the investment policy of the government, aimed at increasing the volume of investments in the economy, are mainly related to application of new criteria for encouragement of both foreign and domestic investments and removing bureaucratic barriers. Thus quality administrative service should become an additional advantage of the Bulgarian economy, combined with qualified and low-paid labor force. Application of the **new principle of individual service of an investor with a capital investment of over BGN 100 m**, laid down in the draft encouragement of investments act is already a fact. This has happened even before adoption of the draft amendments to the Foreign Investment Act. The state not only engaged with building the infrastructure to the production site of the new plant of the Turkish company Sisecam in which USD 160 m will be invested, but also provided additional information, consulting and administrative service.

The major positive change in the draft law is the differentiated service of investors depending on the size of investment. The thresholds that determine the attitude of the administration to the investor will be established with the Rules for Implementation of the Act. According to the preliminary announced intentions the envisaged thresholds are BGN 10, 50 and 100 m. Those who invest from BGN 10 to BGN 50 m will be entitled to use already prepared information materials, as well as processed information on potential partners in the country and all administrative procedures for implementation of the investment project. In addition they will use the services of the administration within a minimum deadline prescribed by law. Investors who have decided to invest from BGN 50 to BGN 100 m will use individual information, consulting and administrative service of the investor at all central and local administrations of the bodies of the executive. Investment plans for over BGN 100 m will be rewarded with individual service and **cooperation for building the technical infrastructure related to the object of investment**.

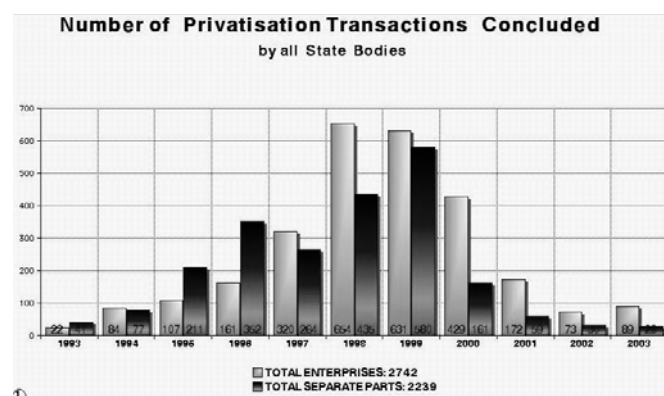
A problem to the pursuit of active policy and actual attraction of foreign investors is the sluggish privatization of big state-owned enterprises. During the review period expectations for concluding offset deals (binding a public procurement order with local production) did not materialize. As a result **the trend toward lower new investments at the expense of market and production expansion of already operating foreign companies sustained**.

## Privatization

**The pace of privatisation in the state sector continued to be unsatisfactory in the fourth quarter of 2003.** Thirty-eight deals for sale of companies with majority (over 50 per cent) state interest and 13 autonomous parts were concluded. Thus at the end of the year execution of the Annual Plan for privatization of

majority blocks of shares is 61.4 per cent. Execution in terms of sale of minority blocks of shares is even worse: 229 deals were concluded and execution of the Annual Program is 25.4 per cent.

Figure 8. Privatization transactions in Bulgaria January 1, 1993 –December 31, 2003



Source: PA

During the review period the process of selling the residual minority state stakes through the stock exchange accelerated, aimed at gradual utilization of the available free nominal value of compensatory instruments and investment vouchers. Unfortunately, there were few attractive enterprises for investors.<sup>2</sup>

In regard to the **revenue side**, execution of the program is unsatisfactory. According to PA data, as of 31 December 2003 contractual payments under privatization transactions amounted to BGN 458.998 m, i.e. 83 per cent of the projected minimum revenue of BGN 550 m.

The above results reveal the weakness of the government in the privatization field. Results from 2002 and 2003 are negative enough to provoke the negative assessments of EC officials and EC<sup>3</sup> official documents on Bulgaria. The privatization process is one of the five basic remarks of the European Union, reflected in the Report on the country's progress in the accession process.

In November investment intermediaries for **the privatization of the Bulgarian Sugar pool and the 30 per cent of Bulgarian River Shipping (BRS)** were approved. In December the deadline for purchasing tender documentation for the privatization of electricity distribution companies expired. Serious requirements to potential buyers guarantee competition and improved efficiency in the industry, although from a consumer point of view it is difficult to judge now how the changed market structure will impact the market price of electricity.

<sup>2</sup> For more details on bourse privatization see the Capital Market section.

<sup>3</sup> On his first visit to Bulgaria the Director General of Economic and Financial Matters of the EC pointed out that "By the time of publication of the next report of the European Commission on Bulgaria's progress in the process of integration the privatization of BTC, Bulgartabac and electricity distribution companies must be completed." Delay in privatization continued in the review period.



The big event in privatization in the fourth quarter was the **Strategy for Privatization of Bulgartabac Holding** adopted by the National Assembly, which was discussed positively mainly by potential investors in the industry. The adopted strategy has the potential for supporting specific regions in the country, enhancing competition in the industry and increasing exports of tobacco and finished products. Also, it is **not immune to threats to the implementation of the objectives set** in it at least for three serious reasons: first, there are no clear deadlines; second, there is no information campaign to report the results from its implementation; and third, there is no pre-set mechanism for allocation of resources among the funds intended to be established, in which the funds from the privatization of individual factories will be received. If materialized, the last threat could have adverse impact on the social effects from the privatization of the Holding. By the end of December a competition for investment consultant on the deal was announced and determined in the first quarter of 2004 – Morgan Stanley&Co Ltd.

At the end of 2003 the Ministry of Economy initiated gathering of **proposals for amendments to the Privatization and Post-Privatization Control Act** from among various organizations and experts. The purpose is to remove legal and political obstacles to the “big privatization.” The proposals will be subject to public discussion. The initiative will be useful if it receives the political support of the National Assembly, for the PA Plan for 2004 proposes for a third successive year one and the same companies for privatization: BRS, MNB, Teraton EAD, Kintex, Bulgaria Air, Bulgartabac Holding AD, Vazov Machine Building Works EAD of Sopot, and the seven electricity distribution companies.

The expected number of transactions for companies with majority state stake is reduced to 119, and expected revenues amount to BGN 500 m.

**The Privatization Agency intends to continue offering companies on the stock exchange**, determined by the government for privatization with non-cash instruments of payment. According to PA data, for a year and a half compensatory instruments used in bourse privatization amount to approximately BGN 300 m nominal value, or over 28 per cent of available bills and notes. The goal of the institution is to raise the price of non-cash instruments of payment by offering new minority blocks of shares on the stock exchange and to optimise revenue and shorten the term for sale by offering majority blocks of shares of state-owned companies.

Out of the total number of companies to be offered for sale in 2004, in 60 per cent of them the preparation for privatization has not begun yet, in 18 per cent some preparatory work has been done, and a mere 8 per cent of the companies are at the final stage of preparation of tender and competition documentation. These facts do not give certainty that the work of the PA in 2004

will be more successful. The PA does not provide any official information in its annual privatization plan about the other 14 per cent of the companies with majority stake.<sup>4</sup>

## Access to financing

During the last quarter opportunities for financing of enterprises increased further. **New amounts under pre-accession funds** were negotiated and for the period 2004 - 2006 the total amount will reach EUR 1.2 b, or some 6.5 per cent of Bulgaria's annual GDP. However, these figures may prove unachievable owing to the sluggish work of the administration in utilizing the funds and the poor programs for training of entrepreneurs on the possibilities provided by pre-accession funds. The other aspect of the problem is the general impression of the poor quality of investment projects submitted by entrepreneurs for financing. This is yet another niche for improving the work of the administration (specifically the new structures of the Agency for Encouragement of Entrepreneurship), professional and other NGOs in respect of the initiatives for training of entrepreneurs. The conclusions about pre-accession funds apply to the same extent to the funds under the **financial framework set for Bulgaria in the EU budget** for the period after 2006.

Poor utilization of funds and insufficient work by the state in establishing a guarantee fund for micro lending led to an **initiative for establishment of entrepreneurship fund for micro lending to SME** in October. It will be accumulated by deductions from the funds of almost 4 000 members in the Union for Economic Enterprise. The idea is for the fund to start up with BGN 3 m initial capital and to extend credits of up to BGN 20 000.

The opportunities of households and businesses for **access to credits from the banking system also increased** in the review period, confirmed by the higher amount of newly contracted credits (by 38 per cent in 2003 as a whole) and the lower interest rates on short- and long-term credits. Although this has adverse short-term impact on the trade balance, enhanced access to financing provides good opportunities for expanding entrepreneurship, investments and exports of Bulgarian enterprises. A discussion about the advantages and disadvantages of credit expansion of the banking system is underway. Generally, it can be assessed as positive for Bulgarian entrepreneurship. Credit expansion probably contributed to the growth in industrial production and industrial sales in the last quarter.

**The European Day of the Entrepreneur** was held in Sofia at the beginning of October. This initiative could be assumed as an attempt by the government to popularize the work of the new team of the Ministry of Economy and the new opportunities for financing provided by the Sofia Municipality to SMEs on its

<sup>4</sup> See <http://www.priv.government.bg/cgi-bin/ap/07/loader.cgi?k=0>

territory. Establishment of a municipal guarantee fund for micro lending is planned, aimed at financing SME projects. The Sofia City Council approved the framework agreement on this fund in December and the fund will guarantee credits of up to BGN 20 000 and by exception, up to BGN 100 000.

An interesting idea for amending the Encouragement of Investments in SME Draft Law was discussed in December - proposals for amending and supplementing the Encouragement of Investments in SME Draft Law tabled in 2003 by the Bulgarian Stock Exchange – Sofia AD. The proposals involve editing Art. 4 of the SME Act and introduction of a new provision in the Public Offering of Securities Act for **establishing (to the Unofficial Market) a special market for trade in shares and bonds of small and medium-sized enterprises** under the SME Act.

During the review period there were wide-ranging discussions about the funds planned outside the spending side of the budget, to be invested in the economy. These funds are disputable due to their extrabudgetary nature. At the same time, the eventual **fiscal expansion in support of raising the quality of the infrastructure in Bulgaria** contains serious opportunities to intensify entrepreneurship in the economy and should be assessed positively.

## Innovation policy

In December the Bulgarian Industrial Association (BIA) and the Agency for Analyses and International Development launched a joint **Innovations in Business project**, envisaging creation of database with BAS scientific research to facilitate access to information and communication technologies for enterprises after their transfer to production activities. On the one hand, this will have a long-term effect on the supply of applied scientific research and, on the other hand, will encourage companies to seek their integration. As a result corporate competitiveness in Bulgaria will improve in the long run. It is planned for the database to be extended with research from scientific institutes and universities. Entry into force of the Encouragement of Scientific Research Act in October also provides opportunities for more research and applicable scientific developments and hence wider access to ICT for Bulgarian companies.

Bulgaria's participation in the European Program eContent<sup>5</sup>, building a scope for transfer of experience between different administrations in the area of electronic government (through the national competition for achievements in the area of electronic government), as well as extensive use of Internet as a medium for concluding transactions are indicative of the gradually improving access of the companies in Bulgaria to information and communication technologies.

## Efficiently functioning markets

**The new structure of the Commission for Protection of Competition**, determined officially with the effective as of October new Structural Regulation, gives signs of improving the activity and protection of efficiently operating market structures in the economy. Three functional units (directorates) to be specialized in specific activities for protection of competition will replace the existing sectoral structures: "Antitrust and Concentrations," "State Grants" and "Unfair Competition." As a priority the CPC will analyze sensitive sectors with existing monopoly position and agreements between companies leading to suspicion about cartels. These sectors, specified by the EC, are steel production, production of cement, fuels, beer, media advertising and tourist services. Concurrently a positive practice is introduced for training the business in competitive behavior by conducting a number of meetings with professional organizations to explain when and under what conditions relevant legal relations should be regulated by the Commission.

Several heavy fines were imposed (of BGN 100 000) to companies using sales promotion, the awards of which exceed many times the price of the advertised item. The sanctions imposed in 2003 total BGN 1.3 m and BGN 904 000 only in the last three months. The heaviest fines were imposed for illegal agreements between insurers for a fixed price of the green card, the Association of Bread Producers, Sofiiska Voda, Metro Cash&Carry, Zagorka, Coca-Cola. This gives ground to assume that the structural and personal changes in the Commission are appropriate and will lead to its more efficient intervention for protection of competition on domestic markets.

## Preparation for the single European market

**Requirements to the enterprises for compliance with EU legislation** boosted investments in particular industries. According to data quoted in the press, investments in the pharmaceutical industry amount to over EUR 100 m (for the period January – October). The same tendency could be expected in other industries in which enterprises consider the country's EU membership as a long-term priority. Individual organizations run trainings on compliance with the requirements of the European legislation, which may be interpreted as an attempt by the Bulgarian enterprises to meet the requirements of the single market. Such trainings, organized not by the government but by professional organizations, were conducted in the textile industry, whose share in the country's exports is expected to account for USD 1.5 b on an annual basis (or about 15 per cent of the country's total exports in dollar terms).

**The ME once again adopted a wait-and-see attitude regarding communication of the requirements of the single market to the business.** Acquaintance of enterprises with these requirements is an important condition for enhancing Bulgarian companies' competitiveness. According to the EC report on Bulgaria issued in November, Bulgarian companies

<sup>5</sup> See the High Technology and Communications section.

still cannot respond to the competitive pressure of market forces in EU. According to a survey by Alpha Research conducted in October, companies in Bulgaria rely mainly on tax reliefs to free funds for investment to cover the single market criteria (88 per cent of respondents) or on funds from pre-accession funds (60 per cent). Only 15 per cent are oriented toward restructuring and/or consolidation with other partners. From a long-term point of view restructuring and consolidation are the most profitable ways for enterprises to generate more investments. This is so because in the first case companies' internal resources are organized on a productivity principle (i.e. reliance on intensive growth of the company, not on increased amount of invested funds) while in the second case the effect is generated by the scale through reduction of general expenses of consolidated enterprises and freeing more funds for investments.

**Introduction of European standards** in production continues, creating stimuli for innovation among producers. The government adopted a **Regulation on the specific requirements and labeling of milk and dairy products**, which obliges milk- processing enterprises to introduce new markings on the packets of their products within one year. The purpose of this regulation is to create conditions for better customer awareness and consumer protection.

All enterprises for production and processing of foodstuffs from animal origin (meat, milk, fish, and bee) have been examined and assessed in terms of the possibilities to meet EU veterinary and sanitary requirements. It is already clear that about 300 of these will have to be closed since early 2004. The reason is that they have done nothing to improve their production so far and have no technological potential to meet the requirements. These enterprises are a source of unfair competition due to the fact that they do not comply with the requirements and sell at dumping prices. The State Veterinary and Sanitary Control has issued an order on their closing but the procedures for closing the enterprises have not been specified yet.

Other group of enterprises will be temporarily closed which, though having potential to improve their production, have not made the required investments so far. After their temporary closing in the period January – March 2004, when specific prescriptions will be given for the necessary measures and examinations will be carried out for availability of developed business plans for production restructuring, the measure against them will be determined. For most of the enterprises that have prepared plans for restructuring deadlines are set by the end of 2005 to complete their restructuring.

Three fish enterprises obtained the right to export fish products to the EU since early December, whereby **Bulgaria was included in the list of countries which may export fresh fish to the EU member states.**

## Trade policy

Following entry into force in September of the **Free Trade Agreement** with Albania, two more agreements were signed: on 16 October 2003 with Bosnia and Herzegovina, and on 13 November 2003 with Serbia and Montenegro. Along with this consultations with Moldova started for signing a FTA. Thus the country is fulfilling its commitments under the Stability Pact for creating a network of bilateral FTAs with the Balkan countries. In practice these are steps toward creating a free trade zone on the Balkans. This will have a strong positive impact on the opportunities for exports, generated for Bulgarian enterprises. After the series of agreements, agreements between Albania, Bosnia and Herzegovina, Bulgaria, Macedonia, Romania, Croatia and Serbia and Montenegro were signed in Rome in November, providing for the lifting of customs duties for all goods with the exception of agricultural ones. However, a multilateral agreement among the countries has not been signed yet, which would formalize the establishment of a free trade zone.

**The new Rules for Implementation of the Customs Act**, effective as of 1 November 2003, aim to relieve customs formalities (especially with regard to transit). They provide opportunity for declaring the goods via electronic means – submitted customs declarations are certified directly, without signature and stamp, and this will facilitate companies immensely. Only the Sofia City Customs is ready for such electronic declaration but it is expected from early 2004 the option to be accessible in the offices of the five regional customs directorates.

**Changes in the Customs Tariff for 2004** will be consulted with the representatives of business, which is a positive practice for boosting trade and deriving trade policy from the problems and experience of real business.

Producers and exporters of perfumery and cosmetics were severely hit by the **unilaterally introduced by Russia indicative import prices**. According to Bulgarian producers the introduced indicative prices exceed many times the value of the goods. This leads to a multiple increase in the customs fees and eventually to higher prices of Bulgarian cosmetic products. The measure affects all exporters to the Russian market but Bulgarian producers are hit very severely owing to the fact that over 50 per cent of their products are exported to Russia. Moreover, as a member of the WTO Bulgaria may not introduce similar measures on a reciprocal basis as these are forbidden by the WTO. Besides, producers and exporters' planning is severely inhibited by the frequent change of the rules on this market.

**Canada introduced temporary customs duties of 74.6 per cent for import of hot-rolled iron from Bulgaria** as a protection measure against dumping. However, import of Bulgarian products in Canada is negligible compared to other countries and could not affect the domestic market. Only Stomana Industry AD operates on this market and the company

hopes that the currently proceeding inquiry will be terminated and the country will be removed from the list of countries accused of dumping because of non-existing margin.

## Administrative and regulatory environment

The issue of facilitating business start-up and development is particularly important for the further encouragement of business environment in Bulgaria. According to the results of the **Global Competitiveness Report 2002-2003**<sup>6</sup> Bulgaria ranks 62<sup>nd</sup> by the indicator administrative barriers to the business and 79<sup>th</sup> by the indicator administrative barriers to start-up companies (out of 102 countries), which shows substantial possibilities for improvement in this element of the business environment. Efforts to improve the administrative environment did not lack in the review period, but nevertheless of note is the fact that the government does not pay sufficient attention to the institutional stimuli for increasing economic growth and business activity.

This is also evident from the implementation of the **effective as of 18 December 2003 Restriction of Administrative Regulation and Administrative Control on Economic Activity Act**. As mentioned in the previous quarters, this act is unique in the Bulgarian practice for several reasons: first, it contains a requirement for preliminary assessment and analysis of the impact on the environment or behavior of affected entrepreneurs at introduction of licensing or registration regime; second, it introduces tacit consent for issuance of certificates or permits; third, it introduces the principle of the one-stop shop service; fourth, a list of 39 activities that may be subject to licensing is attached.

It should be noted that the effect of the act is yet to be achieved. The act was adopted early in the year and a six-month term was provided in which all government agencies had to review their acts and adjust those that contradict the law. Unfortunately, many institutions did not do the necessary to comply with the requirements of the law. Of essential need is to review the regulations on the economic activities of municipalities.

**The principle of tacit consent**, which has a strong positive impact on entrepreneurship, cannot be implemented currently in its full format. The reason is that it requires harmonization of a number of by-laws and rules for regulation of the activities of specific institutions. Thus any concerned person may challenge in court the by-laws which contradict the law. This can be done in the following cases: when introducing a licensing or registration regime for conducting economic activity by a by-law, if the by-law requires from the economic subject to submit a document of another administrative body for verifying circumstances that have been already certified by that body and registered in the public register; if the by-law establishes requirements for economic activity; if the by-law establishes burdens restricting

competition. The problems with the implementation of the law are yet to surface. It is possible, instead of meeting the deadlines for making a decision, from fear that the principle of tacit consent would not take effect, some officers may attempt to stop the execution of transactions and actions of entrepreneurs. This would lead to appeal and increase of the legal suits on this occasion, which will burden the business with additional costs on compliance with the effective legislation. However, the long-term effect will be positive.

It is possible that the business may challenge the municipalities in court, given the **absence of one-stop shop service**. According to data of the National Association of Municipalities in the Republic of Bulgaria, there are 70 one-stop shop services out of 264 municipalities in Bulgaria. There is a shortage of funds for implementation of this requirement – it requires availability of computers, their connection into a network as well as overcoming a number of other difficulties of financial, organizational and administrative nature.

Overall, it should be noted that entrepreneurs are not well acquainted with the law, i.e. they do not know the rights and obligations presented by it. This holds true especially for the small and medium-sized business, which cannot benefit from the provisions of the law. For this reason entrepreneurs should be more active in their familiarizing with it. Finally, the law is a framework. A number of specific steps are needed for its implementation, aptitude by the business and efforts by the administration for its observance.

## Public procurement

**The Economic Policy Commission to the National Assembly continued discussing at second reading the Public Procurement Act** in the fourth quarter. The Act was adopted at first reading in September 2003 but its adoption at second reading was considerably delayed. The reason is that it contains disputable texts.

The European Commission criticized the draft law on several major points. Firstly, the EC objects the preferences for Bulgarian companies included in the version of the discussed act. The draft law contains preferences for Bulgarian companies if the offer submitted by them is 15 per cent higher than the lowest offer of a foreign company. It is envisaged for this scheme to apply only to countries that do not ensure evenhanded access of Bulgarian companies to their public procurement. The draft law provides for the preferences to take effect as of 2004 and to gradually decrease by 5 per cent per annum until 2007. In practice, the proposals would not restrict access of companies from the EU to Bulgarian public procurement. Nevertheless, the EC objects in principle to possible preferences.

<sup>6</sup> World Economic Forum. The Global Competitiveness Report 2002-2003, p. 399



However, preferences for Bulgarian companies upon awarding of public procurement are one of the proposals actively supported by the representatives of the local business.

The second major point of objection by the EC is the status of the Public Procurement Agency. According to the draft law, the Agency must have a status of an executive agency to the Ministry of Economy. According to the EC experts, the Agency should be a fully independent institution from the executive. A possible option is for the Agency to be an independent entity similar to the CPC and the Financial Supervision Commission and its members to be elected directly by the National Assembly. An important function of the Agency will be the solution of disputes under the PPA and exercise of control on the transparency of the procedures for awarding public procurement orders.<sup>7</sup>

A point of discussion in the Act is the solution of disputes on public procurement orders. It is envisaged that annexes to the contracts for execution of public procurement orders to be forbidden so that procedures should not be discredited. The ground is that through the annexes the contracting authority and the selected contractor may agree on more favourable conditions in deviation of the already set ones. Measures are proposed to eradicate the practice of discrimination and privileges to some participants by the contracting authorities.

At the end of 2003 the **National Assembly adopted an amendment to the effective Public Procurement Act**, whose economic effect is aimed to stop the vicious practice applied by some budget-supported institutions of declaring massively public procurement orders for supply of goods through the commodity exchange, but that happens usually at the end of the year when these institutions spent saved funds hastily and in many cases uncontrollably.

However, the new text has both some positive aspects (reducing the irrational spending of budget funds) and possible weaknesses. The amendment may have an adverse effect mostly on bourse trade which has many advantages – swiftness, optimum price and few options for “blackmailing” of the participants. According to data announced in the press, public procurement orders account for 60 per cent of the turnover of the Sofia Commodity Exchange AD. The turnover is valued at BGN 312 m for 2003<sup>8</sup>. A great number of organizations use the exchange for awarding public orders, including ministries and municipalities.

## Fighting corruption

Requirements to the business associated with the process of accession to the EU increase. At the same time costs for

compliance with the effective legislation do not decrease and in this context the administration continues posing problems to the business. According to a **study** by Vitosha Research conducted in November over 60 per cent of the companies have offered a bribe to an officer of less than BGN 250 in order to obtain a license and 38.5 per cent of the companies have offered a bribe of BGN 1 000 to BGN 5 000 to resolve a suit in their favor. This poses serious issues to the necessary changes in the legal framework, mainly for restricting administrative regulation and activities of the judicial system. Overall, of note is the fact that the business criticizes corruption practices on the one hand, but is susceptible to making use of them in one way or another, on the other hand.

In December Coalition 2000 presented the results of the study and the corruption indexes calculated on the basis of polling 421 business organizations, conducted in October – November 2003. According to the study, regardless of the slightly lower values, corruption continues to be identified as one of the major problems faced by the business. Corruption pressure and expansion of unofficial payments has intensified. These phenomena are spread in lending and obtaining construction permits. According to data from the Coalition, in the last two months the share of corruption practices related to tax payments doubled. Most often companies gave bribes to avoid a fine for violation committed by them. Another critical aspect is related to unofficial payments under the procedures for awarding public procurement. According to the study, 42.1 per cent of the polled managers have stated they had paid unofficial sums in winning a public procurement order. The conclusion is that representatives of the business are increasingly tempted to offer or give a bribe for winning a public procurement order. According to 39 per cent of the respondents, the government does not take efficient measures for fighting corruption.

The report of Coalition 2000 on the spread of corruption based on corruption monitoring among the population shows that “small” corruption has become a massively spread phenomenon – 83 per cent of the bribes given in the last quarter amount up to BGN 100 and their share has increased by 18 per cent over the year. So-called “small corruption” has become an ordinary mechanism for settling relations between individuals and public servants, according to the study.

In the fourth quarter a **“Civil Convention on Corruption” was promulgated**, signed by the member countries of the Council of Europe and the other EU member states, ratified by Bulgaria and effective as of 1 November 2003. The Convention lays down general concepts related to the definition of corruption and providing efficient arrangements in each country for the persons that have been harmed as a result of acts of corruption, allowing them to protect their rights and interests.

Another event contributing to improvement of the business environment in the country was the **conference entitled**

<sup>7</sup> Before adoption of the new act, in February 2004 the CM by a decree took a decision on establishing an Executive Public Procurement Agency to the ME.

<sup>8</sup> Source: Sofia Commodity Exchange AD, Annual Report 2003.

**“Overcoming Corruption – A Factor to Improve the Business Climate in Bulgaria,”** held in December. The Conference is a good example of joint actions of entrepreneurs and government administration. The Conference was organized by the Commission for Coordinating the Work on Corruption Fighting and BIBA. The Commission briefed the participants on the results of the analysis of received signals for corruption and the measures taken and BIBA presented its White Book and proposals for solving a number of problems related to corruption practices. The Restriction of Administrative Regulation and Administrative Control on Economic Activity Act was discussed as well as the expected effects of its implementation.

Major events in the area of public finance in the fourth quarter of 2004 are associated with the good execution of the consolidated fiscal program, a balanced budget achieved for the first time since 1999, an ongoing decrease in the debt/GDP ratio, adoption of Budget 2004 and changes in tax laws.

### Execution of the budget in the fourth quarter of 2003

*Consolidated budget (covers the national budget and all autonomous budgets – those of local governments, insurance funds, state universities, Bulgarian Academy of Science, Bulgarian National Radio, Bulgarian National Television, Supreme Judicial Council, as well as extra-budgetary funds and accounts on central and local level).*

According to data on the fourth quarter, execution of the consolidated fiscal program for 2003 is very good. According to MoF data as of 31 December 2003, a **surplus on the consolidated fiscal program** was generated for the first time since 1999, totalling BGN 0.937 m. As a result the agreements with the IMF of the fall of 2003 on achieving a balanced budget were fulfilled.

**Revenues** and aids by the end of December 2003 amount to BGN 14 072 m, little over 105 per cent of the total annual amount planned in the consolidated budget program (BGN 13 373.8 m). By comparison, in the fourth quarter of 2002 revenues under the consolidated budget amount to BGN 12 523.3 m or 100.9 per cent of the planned total annual amount. **Expenditures** for the period amount to a total of BGN 14 071 m, or 103 per cent of the annual amount of expenditures under Budget 2003 (BGN 13 636.6 m). By comparison, for the same period of last year these accounted for BGN 12 732.7 m (100.6 per cent against budget estimates). The trend of the recent years of spending sizeable portion of the expenses budgeted in the consolidated fiscal program at the end of the year sustained in 2003. Some of the major items of expense in the fourth quarter were the funds for financing the National Health Insurance Fund, the unpaid expenses for the delegated state activities to municipalities, the Christmas benefits for pensioners, and an extra salary for the persons employed in the budget sphere.

Table 6. Execution of the consolidated fiscal program by year (BGN m)

Indicators	1998	1999	2000	2001	2002	2003 program	2003 report
Revenues	8 906.9	9 689.5	11 063.7	11 837.4	12 523.3	13 373.8	14 072
Expenses	8 620.3	9 649.6	11 233.8	12 017.3	12 732.7	13 636.6	14 071
Deficit/surplus	286.7	40.0	-170.1	-179.9	-209.5	-262.8	0.9

Source: MoF.

*National budget (comprising the central budget, budgets of ministries and agencies and the budget of the Audit Office)*

As of 31 December 2003 a **deficit is reported in the national budget** at the amount of BGN 110.6 m. Revenues into this budget amount to BGN 8 441.6 m (110.2 per cent of the planned for the year), and expenditures total BGN 8 552.2 m (106.6 per cent of the annual amount against 2003 budget estimates). By comparison, last year these values were respectively BGN 7 289.4 m in revenues (104.4 per cent of the planned) and BGN 7 600.7 m in expenditures (101 per cent of the program).

### Central budget

In 2003 the **deficit** on the central national budget amounts to BGN 126.8 m: revenues to BGN 6 743 m, expenditures to BGN 1 123.8 m, and net transfers provided by the CB to BGN 5 745.9 m.

Fiscal reserve (covers cash in BGN and foreign currency on all current and term deposits with the BNB and commercial banks of the central budget, the budget funds of ministries and agencies, the National Social Security Institute, the National Health Insurance Fund and their extra-budgetary accounts and funds, as well as other high-liquid low-risk financial assets in foreign currency of the government).

**The fiscal reserve** at the end of December 2003 decreased by BGN 886.3 m on the previous month and amounts to BGN 3 848.8 m, out of which deposits in BNB account for BGN 3 280.1 m, and foreign exchange assets amount to BGN 2 289.3 m. Table 7 illustrates the dynamics of the fiscal reserve over the period under review.

Table 7. Indicators of the fiscal reserve (FR) according to the Agreement with IMF (BGN m)

	As of 30 September 2003	As of 31 October 2003	As of 30 November 2003	As of 31 December 2003
Total amount of FR	4 450.5	4 546.6	4 735.1	3 848.8
FR funds in BNB deposits	3 831.5	3 970.8	4 176.6	3 280.1
FR funds in foreign currency assets	1 871.6	1 816.6	2 226.7	2 289.3

Source: MoF data

### Municipal finance and fiscal decentralization

As of 31 December 2003 municipal budgets reported a **surplus** of BGN 5.5 m with revenues of BGN 1 390.2 m, net transfers of BGN 795 m and expenditures of BGN 2 179.7 m. At the end of the year unpaid expenses of municipalities on delegated activities were covered in accordance with the agreements.



## Revenue part of the national budget

Overall as of 31 December 2003 surplus on tax revenues to the national budget (107.8 per cent against budget estimates) is lower than the average surplus on budget revenues and aids (110.2 per cent) and non-tax revenues (117.3 per cent).

### Tax revenues

**Tax revenues** in 2003 amount to BGN 6 571.3 m against BGN 5 436.7 m at the end of 2002. Their execution is 107.8 per cent against the annual revenues planned in the State Budget Act for 2003. As of the end of the fourth quarter of 2002 execution of tax revenues to the national budget was 99.7 per cent. Taxes with a comparatively small share in total revenue account for the best execution against the budget program. These are the dividend and income tax, (175.7 per cent), customs duties and customs charges (128.4 per cent), personal income tax (118.8 per cent), corporate income tax (113.7 per cent).

Among **tax revenues**, **VAT** accounts for the highest relative share: 47.2 per cent against 49.5 per cent for the same period of 2002. The trend toward lower share of VAT revenues in 2003 compared with the previous year is in contradiction with the stated government intentions for a gradual increase of the share of revenues from indirect taxes in total tax revenues ("Tax Policy 2003 – 2005"). Execution of VAT for 2003 is BGN 3 100.8 m (105.4 per cent of planned VAT revenues for the year), against BGN 2 690.2 m in 2002 (96.8 per cent of the planned total annual amount). Comparatively better execution on last year is mainly due to increased VAT revenues from imports.

Revenues from **excise duties and charges on liquid fuels** account for a significant relative share – BGN 1 543.9 m or 23.5 per cent of total tax revenues (BGN 1 312.3 m or 24.1 per cent of total tax revenues in 2002). The lower share of revenues from excise duties and charges on liquid fuels in 2003 compared with the previous year is in variance with the stated intentions for a gradual increase of the share of revenues from indirect taxes in total tax revenues in the Tax Policy 2003 – 2005. Execution of the tax compared to annual estimates is 102.8 per cent in 2003 against 95.1 per cent at the end of 2002. Revenues from excise duties are formed mainly from the taxation of two major commodity groups – liquid fuels and tobacco products. The reasons for the growth in revenues from excise duties and charges on liquid fuels in 2003 are increased production of liquid fuels in the country and higher excise rates for petrol and gas oil effective as of 1 January 2003.

The relative share of revenues from **corporate income tax** as of 31 December 2003 (BGN 992.2 m) is 15.1 per cent of tax revenues against 9.4 per cent in the previous year (BGN 510.3 m). Compared to the annual estimates, their execution

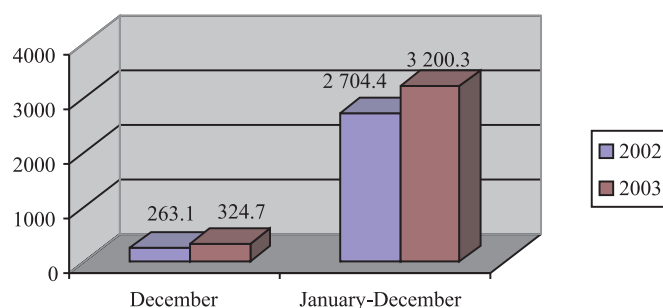
is 113.7 per cent. The significant surplus on the revenues from corporate tax planned in the budget is due to the growth in profits for 2002 of some of the non-financial enterprises as well as to the good financial performance of banks reported for the same period.

The share of revenues from **personal income tax (PIT)** by the end of December is 6.8 per cent of the tax revenues against 9.8 per cent for the same period of last year. The execution of PIT on a net basis is BGN 445.6 m or 118.8 per cent against the annual estimates. For last year collected revenues amount to BGN 531.7 m or 98.3 per cent of the estimates for the year.

Total revenues from VAT, customs duties, excise duties and fines collected by the Customs Agency on the cash basis execution of the national budget for 2003 amount to BGN 3 200 m, or 112.8 per cent of budget estimates (Figure 9). Compared with 2002, generated revenues in 2003 are higher by BGN 495.9 m or 18.3 per cent.

Revenues from **customs duties and charges** amount to BGN 231.3 m or 128.4 per cent against annual estimates. Their increase on 2002 is BGN 42.9 m or 22.8 per cent. The cash execution of **VAT from imports** in 2003 amounts to BGN 2 799.3 m. The increase on 2002 is BGN 394 m, or 16.4 per cent. The execution accounts for 109.6 per cent from the planned amount. The relative share of VAT from imports in total VAT revenues in the country makes up 91.3 per cent for 2003 against 90.2 per cent in 2002. The cash execution of **the excise duties from imports** (net amount) in 2003 accounts for BGN 161 m and is higher by 53.6 per cent (BGN 56 m) than collected excise duties in 2002. The execution is 156.3 per cent against the amount planned by the Ministry of Finance.

Figure 9. Net revenues to the national budget contributed by Customs Agency (cash execution, BGN m)



Source: MoF data

### Non-tax revenues and aids

Non-tax revenues to the national budget at the end of the year amount to BGN 1 836 m or 117.3 per cent against the annual estimates, i.e. better performance than tax revenues. A fairly good execution of revenues to the CB is reported from **fines, sanctions and penal interest** (135 per cent of annual

estimates) and of non-tax revenues of ministries and agencies (132.9 per cent of the planned total amount). Out of the non-tax revenues only generated earnings and income from ownership to CB are lower than the amount planned in the State Budget Act for 2003 (91.5 per cent).

### Expenditure part of the national budget

Overall, **budget expenditures and transfers** on the national budget as of 31 December 2003 exceed the annual estimates laid down in the State Budget Act for 2003 by 6.6 per cent. The share of expenditures made on the budget program (102.6 per cent) is lower than the average execution of budget expenditures and aids (106.6 per cent of estimates) and the net transfers from the national budget (117.8 per cent against the planned values).

#### Expenditures

Among items of expenditure on which economies were realized are social and scholarship expenditures (72.7 per cent against Budget 2003 estimates) and interest on external (87.4 per cent) and internal loans (81.2 per cent). A significant overspending occurred in capital expenditures (144.1 per cent against budget estimates) and subsidies (135.4 per cent of the planned expenditures for the year).

**Running costs** (BGN 2 513.2 m) have the highest relative share of 41.4 per cent of total expenditures. These include costs for medicines, fuel and energy, hired services, current repair, as well as defense and security expenditures. Their execution against estimates is 104.3 per cent, or BGN 104.7 m more than the planned amount.

**Interest paid for foreign and domestic debt servicing** by the end of December amounts to BGN 720.4 m, out of which BGN 161.3 m on domestic loans and BGN 559 m on foreign loans. The relative share of expenditures for interest payments for the period accounts for 11.9 per cent of the total budget expenditures (against 13.5 per cent in 2002). The share of actual expenditure to the planned annual interest expenditure is 85.9 per cent and realized savings result mainly from fluctuations in the euro exchange rate to the dollar in the past year.

The share of **expenditures for wages and other payments to employees** (BGN 594.6 m) is 9.8 per cent of total expenditures in the national budget or 100.8 per cent against the budget program.

#### Transfers

Net transfers from the national budget to other budgets amount to BGN 2 474.2 m. The national budget has allocated to municipalities BGN 779.7 m or 185.3 per cent of the total annual amount (against BGN 987.5 m and 135.5 per cent in

2002). Transfers made from the central budget to the budget of NSSI amount to BGN 923.8 m or 97.8 per cent of the annual estimate. The central budget subsidy to the judiciary is BGN 111.8 m or 116.5 per cent of the annual amount.

### Foreign and domestic debt

At the end of the fourth quarter of 2003 **the total government and government-guaranteed debt** is BGN 16 509.8 m at BNB central exchange rates of BGN as of 31 December 2003. Compared to the third quarter of the year the total amount of the debt has declined by BGN 684.9 m. At comparable data the debt/GDP ratio drops down from 48.7 per cent at the end of September to 47.8 per cent at the end of December 2003. Compared to the same period of last year total debt has decreased by BGN 1 670.2 m due to the US dollar depreciation against the euro in the review period and the repayment of principals and interest.

In **dollar terms**, however, government and government-guaranteed debt has increased by USD 417.6 m over the period from the end of the third to the end of the fourth quarter of the year (from USD 10 243.8 m to USD 10 661.4 m according to BNB central exchange rates for the respective dates). This is due to the depreciation of the dollar versus the Euro, as well as to the foreign currency swap effected in November. As of the end of September 2003 dollar-denominated debt was 44.9 per cent of the total amount of the government and government-guaranteed debt, while at the end of December dollar-denominated debt was already 42.3 per cent. As a comparison, the share of Euro-denominated debt increased from 32.4 per cent of the total amount at the end of September to 34.9 per cent at the end of the year (BGN debt marked an increase in the debt structure – from 8.56 per cent at the end of September to 9 per cent at the end of December 2003).

In 2004 the amount of the debt will probably be predetermined again by the dynamics of the exchange rate of the Euro against the US dollar and the changes in the currency structure. In all cases, however, an important indicator remains the ratio of total debt to GDP which will probably keep its trend of progressive decline.

#### Foreign debt

According to data from the Ministry of Finance, at the end of December the foreign debt amounts to EUR 7 295.4 m (against EUR 7 657.4 m at the end of the third quarter of 2003), the government debt accounting for EUR 6 903.1 m (against EUR 7 261.4 m at the end of June) and government-guaranteed debt - EUR 392.3 m (EUR 395.9 m as of 30 September 2003). As a result mainly of the changes in the exchange rates over the period from the end of September till the end of December 2003, the total amount of the foreign debt in dollar terms marks an increase of USD 291.7 m. In BGN terms a trend is observed

toward a reduction of the amount of foreign debt by BGN 708 m. The total foreign debt at the end of December amounts to USD 9 214.1 m or BGN 14 268.6 m, recalculated at the BNB rate of BGN to USD as of 31 December 2003.

In November a **foreign currency swap was concluded with the World Bank** on Bulgaria's liabilities under the FESAL 1 loan "Restructuring of the financial sector and enterprises" for an initial amount of USD 100 m. Payments on principal and interest were converted into euro, with a term from 15 December 2003 to maturity of the loan. The loan amount as of 15 December 2003 is USD 95.8 m. Such an operation would have an economic effect if the dollar depreciates against the euro during the loan repayment term.

As a result of the foreign currency swap slight changes occurred in the **currency structure** of the debt. The Euro-denominated debt reached 36.9 per cent in end-December 2003 from 34.1 per cent in end-September at the expense of the debt in US dollars: 47.2 per cent (against 49.7 per cent in the third quarter). The share of the debt denominated in other currency decreased and accounts for 16 per cent (16.2 per cent in September). **The interest structure** is also subject to very slight change. The ratio between floating interest rate debt and fixed interest rate debt is 62.4 per cent to 37.6 per cent. The average residual term of the debt decreased to 9 years and 10 months compared with the previous quarter. Highest is the share of the debt on other bonds (global and eurobonds): 27.9 per cent and that of Brady bonds (amounting to 25.9 per cent). The share of the debt to IMF slightly decreased to reach 12.9 per cent. Payables to the World Bank account for 11.9 per cent, to EU – 4.8 per cent, on government-guaranteed borrowings – 5.4 per cent, and to the Paris Club – 3 per cent.

#### Domestic debt

As of 31 December 2003, according to Ministry of Finance data, the domestic debt amounts to BGN 2 241.1 m. Compared to the end of the third quarter of the year it marked **an increase of the total amount of domestic debt** by BGN 22.9 m.

Within the structure of domestic debt at the end of December 2003, the share of government securities issued for financing of the budget deficit is 76 per cent (against 74.6 per cent at the end of September) of the total amount of the domestic debt. At the end of December, the share of the debt on government securities issued for the structural reform is 24 per cent (against 25.4 per cent at the end of the third quarter) of the total domestic debt. Table 8 shows the dynamics of the total domestic debt structure.

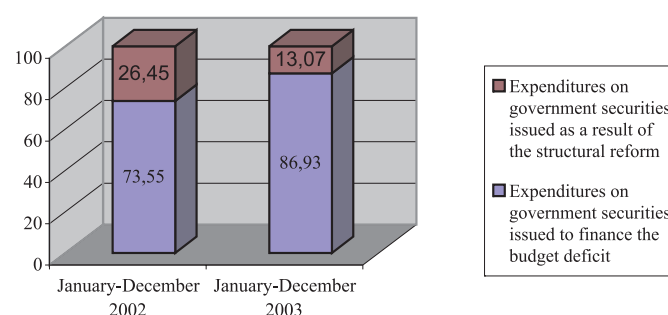
Table 8. Total domestic debt structure (%)

Debt structure	As of 31 December 2002	As of 30 September 2003	As of 31 December 2003
Debt on government securities issued to finance the deficit	69.24	74.6	76.0
Debt on government securities issued for the structural reform	30.67	25.4	24.0
Domestic government guarantees	0.09	0.0	0.0

Source: according to MoF data, Government Debt monthly bulletins.

**Total expenditures on the domestic debt** (interest and discounts) at the end of the fourth quarter of 2003 amount to BGN 118.6 m (against BGN 108.1 m for the respective period of the previous year). Among these expenditures, the share of expenditures on government securities for financing of the budget deficit is 86.93 per cent (against 73.55 per cent at the end of December 2002). Highest is the relative share of expenditures on 5-year bonds (38.7 per cent), followed by those on 7-year bonds (19.4 per cent), and 3-year bonds (19.3 per cent). The share of expenditures on government securities issued for the structural reform is 13.07 per cent (against 26.45 per cent in the same period of 2002). Figure 10 illustrates the dynamics of the structure of expenditures on the domestic debt in 2002 and 2003.

Figure 10. Expenditure structure of domestic debt (%)



Source: according to MoF data, Government Debt monthly bulletins

According to BNB data (Government Securities bulletin of Fiscal Services Department), during the months September - December 2003 **average yield attained in the primary market** on newly issued government securities for financing of the budget deficit is 2.68 per cent on an annual basis for three-month treasury bills (three auctions for the period), 4.9 per cent on an annual basis for five-year treasury bonds (two auctions for the period), 5.48 per cent for seven-year treasury bonds (one auction for the period). No twelve-month treasury bills, three-year and ten-year treasury bonds were issued during the quarter.

At the beginning of November **fifteen-year treasury bonds** in Euro were issued, maturing on 11 October 2018, of EUR 100 nominal value and average annual yield of 6.55 per cent. This is in line with the overall strategy for development of the

internal financial market with a view to increasing the range of instruments offered in it. Securities totaling EUR 20 m in value were offered. The issue is fully standardized with European norms.

Thus, with regard to the domestic debt market, the fourth quarter marks a decrease in the yield of all newly issued government securities compared to the previous quarter (with the exception of three-month treasury bills) and 2002. In comparison to the end of the third quarter the share of securities issued for financing of the budget deficit has slightly decreased at the expense of the share of securities issued for the structural reform. In comparison to last year, the share of expenditures on government securities issued for financing of the deficit increased, while the share of expenditures on securities related to the structural reform dropped down as a consequence of the changed structure of domestic debt.

In November the new **issuing policy of the Ministry of Finance** for 2004 was presented. In the context of the rapidly changing situation on the debt instruments market as well as the desire of the issuer to pursue flexible and adequate issuing policy the Ministry of Finance took a decision to discontinue the practice of announcing annual calendars of government debt issues with specific commitments for dates and volumes of offered securities. For 2004 only the general framework with the intentions for debt issuing on the domestic market was announced and a specific monthly calendar will be provided not later than 30 days before the date of the auction.

In 2004 the Ministry of Finance will offer for sale on auction principle government securities of total nominal value between BGN 650 m and BGN 750 m. The newly issued securities will be in the range of 3 months to 15 years. Short-term government securities will include three-month and twelve-month treasury bills sold at discount of their nominal value. The practice for three-month government securities of offering one issue monthly in the amount of BGN 12 m will sustain. As regards to twelve-month treasury bills, placement of two issues of BGN 20 m each is planned. In 2004 the Ministry of Finance intends to offer five-year bonds denominated in Euro targeted at individual investors – natural persons. These will be sold once monthly and every other month three-year issues in BGN will alternate with five-year issues in Euro. Also, the term for reverse repurchase of the bonds by the issuer is to be shortened from six to three months. Target issues may be repurchased only by natural persons and offer 1–2 percentage point higher yield than that on government securities with the same maturity issued on auction principle.

In 2004 the Ministry of Finance will continue issuing interest-bearing open-end treasury bonds but only one issue of the respective maturity will be placed within the year. Medium-term treasury bonds will be represented by three-year and five-year government securities with respective

volumes of the issues of not less than BGN 100 m.

Long-term treasury bonds will be represented by seven-, ten-, and fifteen-year government securities and their volumes will not exceed BGN 80 m. Specifically with respect to fifteen-year government securities the Ministry of Finance plans to offer for sale up to EUR 100 m of the remaining quantity of issue BG 20 404 03 219 of 12 November 2003, denominated in Euro.



*New financing*

During the year **new loans** received total BGN 847.8 m, against total **foreign debt payments** of BGN 1 410.5 m. The payments include repayment of principals at the amount of BGN 767.4 m., and interest payments of BGN 643.1.

At the end of October 2003 **Financial Memorandum** BG2003/004-937 between the European Commission and the Republic of Bulgaria was signed under the National PHARE Program for 2003. The Financial Memorandum amounts to EUR 94.9 m extended by the European Commission as aid to the Republic of Bulgaria. The financial participation of the Republic of Bulgaria involves national co-financing of the projects with investment component. The funds extended under this Memorandum will be used for implementation of projects in six priority program areas: strengthening of the public administration at all levels and of the judicial system; improving transparency, financial control and fight against corruption and frauds; encouraging economic growth, competitiveness and social cohesion; integration of minorities and vulnerable groups into society and creating a more dynamic pluralistic civil society; enhancing the administrative and judicial capacity for implementation and enhancing legal measures for undertaking some of the obligations upon EU membership; improving strategic planning and efficient use of EU funds and preparation for the structural funds (including application of an extended decentralized implementation system). Selected priorities are based on political coordination between the Bulgarian government and the European Commission.

In December **the results from contracting funds under the PHARE Program 2001** were presented. At the end of the contractual period (30 November 2003) almost 96 per cent of the funds were contracted under institutional building projects and about 93 per cent of the funds in the area of Economic and Social Cohesion and Cross-border Cooperation. For the purposes of institutional building for the first time about 100 per cent of the proposed projects were contracted. Their total value is almost 96 per cent of EUR 43 m (the value of the Financial Memorandum). Due to the lower price bids offered by the candidates under individual projects 5 per cent savings were realized. A key project is that on "Recruitment and training of employees within the judicial system". It will contribute to improving the quality of judges and to the harmonization of the judicial administration with EU requirements. The project amounts to EUR 2 m. Within the National Program Phare 2001 six grant schemes of 423 grant contracts in total were negotiated, amounting to EUR 27.5 m. They finance small-and medium-sized enterprises for consultant services; research and development and technological transfer; non-government organizations providing social services or operating in the field of integrating vulnerable groups; activities supporting the country's accession process to the EU.

On 11 December 2003 the fourth meeting of the Joint Monitoring Committee was held which reviewed and assessed the implementation of the programs and the projects within the programs, financed by the European Union. The meeting reported that the country had made a progress on the pre-accession programs financed by the European Union. Special attention was paid to the good implementation of the projects under SAPARD and the 100 per cent contracting of funds under Phare 2001.

At the end of December 2003 the World Bank disbursed the third tranche of EUR 20 m under the EPSAL loan in support of the national environmental priorities. The EPSAL loan is a structural loan amounting to EUR 49.5 m and has been implemented since April 2000. The loan is in support of the balance of payments and environmental policies as well as of the environmental programs for compensating the damages from past pollutions of privatized enterprises. It supports harmonization of the environmental legislation with that of the EU. The project supports the pilot introduction of integrated permits for protection against pollution as per Directive 91/96 on integrated control of pollutions.

**Regulatory framework development**

In the last quarter of 2003 the **2004 State Budget Act** was adopted and major tax laws were amended: **Corporate Income Tax Act, Personal Income Taxation Act, Value Added Tax Act, Excise Duty Act, Local Taxes and Charges Act.**

*State Budget Act for 2004*

Budget 2004 as a whole is of more expansive nature compared with Budget 2003. The trend of **higher share in GDP of redistributed funds through the revenue and expenditure side of the budget continues**. The higher share of budget revenues and expenditures is not only in contradiction with the government's intentions to reduce state intervention in the economy but also with the specific estimates included in the medium-term program "Tax Policy 2003 – 2005". **Revenues** planned in the national budget amount to BGN 9 111.5 m (BGN 7 660.3 m in 2003). The highest shares in total revenue are expected from social security and health insurance contributions (26.8 per cent), VAT (23.1 per cent) and the personal incomes tax (8.1 per cent).

Planned **expenditures and transfers** amount to BGN 9 376.5 m (against BGN 8 021.6 m under the 2003 State Budget Act). The budget deficit is projected at BGN 265 m (0.7 per cent of projected GDP). The main spending priorities in individual areas include social security, support and care (13.5 per cent of GDP), education (4.2 per cent of GDP), health care (4.3 per cent of GDP), defense and security (4.9 per cent of GDP) and public works (2.1 per cent of GDP). Expenditures on maintenance and salaries of the administration increase as

a share of projected GDP. This is consistent with the need for establishing new structures related to the country's accession to EU and the projected increase of the salaries in the budget sphere by 8.5 per cent in July 2004.

The intentions of the government to invest up to BGN 500 m from the fiscal reserve for increasing the capital of the state-owned company Avtomagistrali, which is to invest jointly with private companies in infrastructure projects, is another controversial aspect of Budget 2004. The funds are in essence of expenditure nature and are recorded outside the expenditure side of the budget under the Financing item. The main criticism is associated with the lack of transparency and the macroeconomic effects of the measure. Such a scheme requires sizeable government guarantees. After the intervention by international financial institutions and local experts it was agreed that the funds will be spent as late as the second half of the year if there are favourable macroeconomic conditions and in accordance with the recommendations of the World Bank on the needs of investment in infrastructure.

Budget 2004 provides for full financing of the expenditures on the state-delegated activities and the planned funds are raised by 0.5 per cent of GDP on 2003. This is a major step toward accelerating the process of fiscal decentralization.

#### *Corporate Income Tax Act*

Major changes in the CITA refer to the manner of forming the tax basis for specific categories of taxpayers as well as the tax rates applied. The concept of a Tax Depreciation Plan (TDP) has been precised by defining the basic concepts and detailing the rules for initial introduction and subsequent keeping of TDP. Of significant importance are changes in tax treatment of amounts reported as a result of events in past reporting periods, corrections of fundamental errors from past periods or changes in accounting policies. The tax effect from transformations is specified as well as ceding of corporate tax.

The amended Art. 44 of CITA provides for a **reduction of the corporate tax rate by four percentage points** (from 23.5 per cent to 19.5 per cent) as of 1 January 2004. The change has a very positive nature as the tax burden on the business is reduced and funds are released for investments in the business and job creation. According to estimates of the Ministry of Finance, reduction of the corporate tax rate will lead to a reduction of budget revenues by some BGN 150 m. **In addition, the regime of taxation of budget-supported enterprises is modified.** The change provides for the introduction of one-off tax on income from economic activity in the amount of 4 per cent.

**A new category VII "Depreciable fixed intangible assets"** for which there are legal restrictions on their use was introduced. The annual depreciation rate for these assets will be determined on the basis of the term of the legal restriction on use and it

may not be higher than 25 per cent. Computer peripherals are added to category IV "Computers and software" (with 50 per cent annual depreciation rate).

The tax treatment regime of the expenses on transportation of personnel made by the employer is relieved. Reported expenses on group transportation of personnel, including employees under management contracts, carried out with own or rented vehicles from the place of residence to the work place and vice versa are not regulated for tax purposes and are not charged with tax at source, with the exception of motor cars. The one-off tax on expenses for donations to organizations listed in the Act (educational and medical institutions, hospitals, the Bulgarian Red Cross, etc.) in 2004 amounts to 15 per cent (20 per cent in 2003).

#### *Personal Income Taxation Act*

Changes in the Personal Income Taxation Act adopted in late 2003 concern the general principles of taxation under PITA and final annual (patent) taxation.

Major changes in the taxation scale under PITA involve **an increase of the tax-exempt minimum** – from BGN 1 320 to BGN 1 440 per annum (BGN 110 to BGN 120 monthly). In addition, the **minimum marginal tax rate** has been reduced – from 15 to 12 per cent. At the same time commitments undertaken under "Tax Policy 2003 – 2005" for updating the limits of the brackets of the income taxation scale in line with the inflation rate and reducing by 2 percentage points the rates for the middle brackets have not been fulfilled. The adopted changes lead to certain reduction of the tax burden on the previous year (mainly for lowest income taxpayer groups) which does not correspond to the initial commitments.

In terms of the **patent tax** the most important change is in the scope of persons subject to patent tax. Annual turnover as a condition for this taxation regime is reduced from BGN 75 000 to BGN 50 000, equalizing it with the threshold for registration under the VAT Act. The change is introduced in order to differentiate the scale of small business and hence relieve the reporting of tax liable persons. This eliminates the paradox for the persons with turnover between BGN 50 000 and BGN 75 000 and paying patent tax, to register under the VAT Act.

Also, partial changes were adopted leading to reduction of tax amounts for a limited range of activities (maintenance and repair of household appliances, equipment, air conditioners, dry cleaning). Production activity is excluded from the scope of activities subject to patent tax. The limitation for catering and entertainment establishments to have not more than 100 seats for consumption is abolished as a condition for patent tax. The change reflects the need to take into account the seasonal nature of most of these establishments.

Of note is the **change in the categorization of populated areas** for the purposes of final annual (patent) taxation. As of 1 January 2004 a requirement is introduced for annual updating of the information on which the categorization of populated areas is based. Also the grouping of some populated areas is changed (Vratsa, Vidin, Kardjali, Silistra, Smolian, Dimitrovgrad, Karlovo, etc.), which leads to a change in tax liability.

#### *Value Added Tax Act*

Major changes in the Value Added Tax Act effective as of 1 January 2004 are related to excluding from supplies within the meaning of VAT Act of gratuitous supplies of goods and services provided by an employer to employees as per Chapter 14 of the Labor Code (social communal service of employees in enterprises). Exempt from VAT are **supplies under projects within international agreements** to which Bulgaria is a party. The provision according to which imports of equipment for the needs of the Ministry of Defense, Ministry of Interior and other bodies of the national security are not subject to VAT is abolished. The motives are that the provision contradicts the principle of *pari passu* of tax liable persons and puts Bulgarian manufacturers of such equipment in unfavorable position.

#### *Excise Duty Act*

The changes in the Excise Duty Act effective as of 1 January 2004 provide for **higher excise duties on petrol, gas oil, liquefied oil gas and cigarettes** in line with the commitments undertaken by the Republic of Bulgaria for achieving the minimum excise levels applicable in the European Union. Excise duties for some of the fuels (petrol for engines; medium oils, including kerosene; gas oil earmarked for processing or incineration in engines and static fuel installations; and heavy fuels other than boiler fuel) is calculated as an absolute amount in BGN for 1 000 litre. For toluene, liquefied oil gas and other gaseous carbon dioxides the excise duty is calculated in BGN per ton.

As of 1 January 2004 the excise duty on cigarettes with filter amounts to BGN 0.004 per piece + 43.5 per cent of the selling price (BGN 0.002 per piece + 40 per cent of the selling price in 2003). For cigarettes without filter the increase is from BGN 0.001 per piece + 15 per cent of the selling price to BGN 0.002 per piece + 20 per cent of the selling price.

With the changes in the Excise Duty Act of 1 January 2004 **the amount of excise duty on cigars and coffee extracts is decreased**, as existing rates were well above the minimum excise duty on these goods in the European Union. This facilitates smuggling and puts correct taxpayers in unfavourable position. Also, the sale of spirits in plastic packaging (bottles) is forbidden. This is aimed to constrain the illegal production and sale of spirits and to protect the interests of correct taxpayers who suffer damages from illegal trade. The excise duty in 2004

will be paid once by the 14<sup>th</sup> day of the month (not twice a month, as is the case now). No excise duty is due or the excise duty paid is refunded for motor vehicles which have been stolen and the due customs duties have been recovered or simplified in accordance with the procedure of the Customs Act and the rules on its implementation.

#### *Local Taxes and Charges Act*

Amendments and supplements to the Local Taxes and Charges Act are aimed at:

- protecting taxpayers against actions by the respective municipality during the year, resulting in higher valuation and tax basis of the real property;
- unifying the time limit for filing a declaration for acquiring a vehicle by inheritance with the other cases of acquisition of property by inheritance;
- abolishing the requirement for the table under Art. 55, para. 1, second sentence – determination of the tax basis for the tax on vehicles - to be changed every year and in the table for the coefficients the year of manufacture is replaced with the number of years from the date of manufacture; the amount of the tax is retained.
- Unifying the administrative penalty regime regarding the powers of mayors of municipalities for issuing penalty acts in relation to the functioning of the National Revenue Agency and the already amended Local Taxes and Charges Act in this regard.

In October a **draft law on amending the State Budget Structure Act** was submitted for deliberation by the National Assembly. It envisages the creation of Chapter Eight "Fiscal Reserve" whereby the National Assembly shall determine the required minimum reserve in accordance with the public nature of the funds. This shall be done annually depending on the condition of the economy, the foreign debt service burden for the country and the medium-term stability of the budget. The minister of finance shall be responsible for the pursuit of a reasonable investment policy. Requirements for restricting the risk are introduced. Public procedures are envisaged for investments in the country's banking sector. Investments may be made only after consultations with the central bank in view of its responsibilities under Art. 2 of the BNB Act as investments have an impact on monetary balances. The draft law provides for the minimum amount of the fiscal reserve with the exception of the funds of the National Fund to be kept by the BNB. The need for transparency in respect of forex and fiscal reserves entails unification of the regime of disclosure of their state through monthly reports.



## Employment and Unemployment. Labor Market Policy

**A negligible increase in the number of unemployed Bulgarians was registered in the last quarter of 2003.** It is more expressed in November and December, thereby breaking the trend of decreasing unemployment observed in all months since the beginning of 2003. Such increase is also conditioned by the end of the seasonal employment period in the tourism and the agriculture sector. But it is not expected to have significant effect on total unemployment. Overall, unemployment levels registered serious decline against the previous year, from 16.27 per cent at the end of the fourth quarter of 2002 to 13.52 per cent in 2003.

The increase in the number of new vacant jobs observed in the fourth quarter as well withstands this negative change. That does not mean that the unemployed automatically find jobs, for age, qualification, geographic and other reasons, but it is a signal of labor market dynamics and of preconditions to gradually overcome the unemployment problem.

An important event in the fourth quarter was **the Strategy for Employment in Bulgaria, 2004-2010** adopted by the Council of Ministers. It is a document based on the objectives of the European Strategy for Employment – full employment, quality of labor and productivity, and a labor market guaranteeing a high degree of inclusion. Permanent decrease of unemployment in Bulgaria to levels below 10 per cent and increase of the economic activity of Bulgarians by not less than 5 percentage points (it is now about 61 per cent) is envisaged, in line again with EU accession requirements. The Strategy takes account of the serious challenges at this stage of Bulgaria's economic and social development – low economic activity, high unemployment, and high relative share of the informal economy. Against this background it contains mid-term and long-term objectives and specific programs and measures to attain them. In the period till 2007 the focus will be mainly on curbing unemployment. The special employment programs of the Ministry of Labor and Social Policy will be expanded with a view to increase employment. The Strategy also contains specific guidelines on how to improve on this basis the economic activity and the labor achievements of Bulgarians by 2010.

Another employment program aimed at ensuring access of women to employment was launched in the last quarter of 2003. The Back at Work Project will train and prepare 400 jobless and/or unemployed women and will improve their employability. This program comes in response to the specific needs of women, who have a high relative share in total unemployed, in total permanent unemployed in particular. Their education level is low, they do not have profession or qualification and very often they are absent from the labor market for a long period on account of pregnancy and raising children till the age of 2 or 3. Women's involvement in special training will increase their chances to find a job and to develop professionally. Within a

program of the Ministry of Labor and Social Policy again, 1000 unemployed nurses will be trained for child raising aids.

The Labor Migration Regulation Agreement between Bulgaria and Spain, signed in October 2003, is an example of a modern approach which takes account of local realities and the European perspectives for Bulgaria's development. This is a broad-scope document regulating the full range of employment and probation, which guarantees the social security rights of Bulgarian nationals.

An Information and Service Center of the Employment Agency became operational in October 2003. It functions on the "one-stop-shop" principle and provides information and consultations on all activities of the Employment Agency.

## Incomes and living Standards

**The fourth quarter of 2003 signals of serious problems for the incomes of Bulgarians and is not an encouraging finale of the year.** After the increase of real incomes (average monthly wage of the employed and monthly income per household member) registered in the previous three quarters, the last three months of the year all but stopped this trend. Thus in October 2003 was registered negative growth of the real average monthly wage of the employed against the corresponding period of 2002; the increase on a quarterly basis is 0.03 per cent, and for the whole 2003 – only 2.2 per cent. According to the household budget statistics, the growth rates of total real income per household member are also considerably lower compared to the previous quarters and against 2002.

The consumption of basic consumer goods follows income dynamics, with incomes of the people living and working in Sofia and the big towns determining consumer market trends. Switch of consumption to cheaper goods and increasingly higher importance of the price as a consumer choice factor is observed.

The objective stagnation processes in the incomes of Bulgarians are also reflected in NSI's regular "consumer confidence" surveys. Late 2003 and early 2004 are marked by increasingly higher pessimism in consumers' assessments of and expectations about the economic situation in Bulgaria, the financial situation of households, the inflation dynamics and the unemployment. The amount of the unregulated additional payments for education and health services is hardly perceptible, but these should be taken into account in projecting the living standards of Bulgarians. **Against this background, the planned increase of the electricity and heat prices and of the excise duty on fuels in 2004 will create preconditions for social tension, negligible expansion or stagnation of consumption and continuing lower standard of living for large groups of Bulgarians in the long run.**

## Social Assistance

**Intensified activity of government institutions in the area of social assistance and the policy on curbing poverty in Bulgaria was registered in the last three months of 2003.**

These topics were obviously in the focus of attention in the period under review and in this case the question is rather about the logical end of a process, which has started earlier, and not about some campaign or a single effort. From now on the challenge will be to effectively implement a large number of strategic and programming documents and to complete them with new and modern forms of social services.

The focus should be placed on the documents regulating the disabled people policy – **the Bulgaria for Everybody National Program, the National Strategy for Equal Opportunities for the Disabled People, a draft law on the integration of the disabled people, Action Plan for the Equal Opportunities for the Disabled People 2003 – 2005, and Disabled People Employment Plan.** This package of documents was developed with some delay, but it is an example of a modern comprehensive approach towards the problem of providing assistance to and full social integration of the disabled people. The documents envisage commitments for all institutions engaged with the problem /the Executive Agency for the Disabled People, teams for integrated training within the general education environment at the regional inspectorates of the Ministry of Education and Science, the bodies of local self-government, etc./, as well as liability for non-fulfillment. Preconditions to integrate the disabled people in the labor market are created through incentives for employers to employ disabled people. Given Bulgaria's enormous delay in this field and the need of more humane attitude towards the disabled people, the requirement and obligation to build an accessible living and architectural environment and to provide access to transport services by the end of 2005 is particularly important.

The efforts of the Ministry of Labour and Social Policy to develop the first Bulgarian **National Strategy for Fight against Poverty and Social Exclusion** should be recognized. The document was drawn up by leading Bulgarian experts with the support of international donors. It is the first step towards clarifying the problem and defining realistically the poverty parameters in Bulgaria. The Strategy was approved in October 2003 and envisaged for the first time introduction of a "poverty threshold" and drawing a map of poverty. It also envisages decrease of poverty and the risk of social exclusion in 2003 – 2006 through facilitated involvement in employment and facilitated access for everybody to resources, rights, benefits and services; assistance for the most vulnerable social groups, and cooperation of institutions, local authorities and the civil society. The Strategy and the National Plan for Fight against Poverty and Social Exclusion are examples of a comprehensive approach and orientation toward prevention rather than reaction to an already existing risk situation, which is a sign of modern

social policy. **According to the Strategy, by 2010 the relative share of permanent unemployed should decrease from 9.6 per cent to 7 per cent, the unemployment of young people should drop down from 35 to 25 per cent, and conditions where not more than 15 per cent of Bulgarians will live below the poverty threshold calculated on the basis of 60 per cent of the average monthly income per household member should be created.**

## Industrial Relations and Social Partnership

**The end of each calendar year is traditionally characterized by more events and higher dynamics in the relationship of employers, trade unions and the State on account of the state budget for the next year, the demands for additional wages and allowances** to pensions, outstanding liabilities towards workers, etc. Such a trend and demands for payment of the wages due emerged in 2003 as well. These were more expressed among teachers, railway workers and road builders, in Terem – Plovdiv, and in the companies within the Bulgartabac Holding.

The trade union activity related to the forthcoming privatization of the electricity distribution companies, the approved Privatization Strategy for Bulgartabac, and the plans to restructure the railways continued. The common thing about all these cases is the higher interest of trade unions in receiving timely information about forthcoming changes and in getting involved in the development of specific documents, with demands focused mainly of preserving the number of work places. Overall, a conclusion can be made that in most cases the necessary conditions for their involvement and for taking into account their opinion are created, in so far as they show restraint and understanding of the economic practicability.

Along with that, the following recommendations towards trade union organizations at all levels can be made: the latter should be more active and watchful with a view to exercise more efficiently their warning functions according to the Labor Code; they should collect and submit on time precise information about labor legislation violations and should increase their presence and control of the health and safety at work.

At the same time, the social partnership in Bulgaria continued and intensified its development. The **Economic and Social Council** was institutionalized and became operational in December. It involves members of the nationally represented workers' and employers' organizations and of non-government structures. The task of the Council is to develop opinions on draft regulations, strategies and analyses of the economic and social policy and to promote the dialogue between the civil society structures and the government authorities.

Approval of Amendments to the Labor Code is pending with a view to introduce mechanisms and procedures to provide

information and consultations to workers and employees in accordance with the requirements of European legislation.

## Social Security

### *New social security aspects in 2004*

The Act on the 2004 Budget of the State Social Security passed in December 2003 reveals that **in the new 2004 higher revenues are expected again in all SSS funds**, owing to the new higher minimum social security thresholds and the expanded scope of insured persons through continued policy of proactive employment measures and of curbing the shadow economy. According to experts, the mandatory registration of labor contracts in NSSI and the higher control on the observation of labor and social security legislation exercised by NSSI and Labor Inspectorate officers are successful measures for fight against the shadow economy.

Despite the expected higher collection of revenues within the state social security system, the 2004 SSS budget **plans higher amount of additional subsidies from the central national budget to cover the deficit – about BGN 576 m for 2004 against about BGN 383 m for 2003**. The 2004 deficit planned for the Pension Fund is also higher compared to 2003 (about BGN 685 m for 2004 against about BGN 479 m for 2003). **Unlike 2003, a deficit to the amount of BGN 44 m is also expected in another SSS fund – General Illness and Maternity**. It is a result of the Parliament-approved decision to have the working days of the temporary disability period, except for the first day to be paid again by the employer, payable by NSSI in 2004. The planned higher deficit in the Pension Fund does not give grounds to expect lower social security burden in the near future.

**In 2004 government officials will be privileged again compared to the workers and employees on labor contracts**. The state will continue to pay the full amount of their social security contributions for the state social security and for the supplementary mandatory social insurance in universal pension funds. **The problem with having the first days of sick benefits paid by employers was solved in part only**. The deputies voted for having the employer pay only the first day of the sick benefit, and not the first three days as before. **The division of the social security burden between employers and employees in a proportion of 75:25 remains valid for 2004 as well**. The social security contributions in the Pension Fund for temporary disability or for pregnancy and childbirth remain for account of the insurer or the self-insured person, which generated great discontent in the business circles.

**Experts give positive assessment of the more detailed specification of the economic activities (from 48 in 2003 to 55 in 2004) employed to determine the minimum social security thresholds for 2004**. This change is a step towards

higher justice and precision in defining the social security burden of employers. The negotiations between employers and trade unions on the new minimum social security thresholds went on wheels, which led to **administrative increase of their amount by 7 per cent** (the increase of the average income for social security purposes in 2003 is also 7 per cent) **for 6 economic activities only**. As a comparison, in 2003 the minimum social security thresholds for 14 of a total of 48 economic activities were administratively fixed. This proves that good cooperation and coordination of trade unions and employers' organizations are in place in the agreement of the minimum social security thresholds. Lower 2004 thresholds were only negotiated for the production of chemical substances, resin and plastic. That was made possible owing to the consensus of employers and trade unions that the economic conjuncture in these sectors does not allow to preserve previous thresholds.

**In 2004 the minimum monthly income for social security purposes of the self-insured persons is preserved at BGN 200. Only the maximum monthly income for social security purposes is increased from BGN 1000 to BGN 1200** as a result of the higher minimum wage (BGN 110 in 2003 against BGN 120 in 2004). In 2004 the minimum monthly income for social security purposes of the registered agricultural producers is also preserved at BGN 100, and the minimum monthly income for social security purposes of agricultural producers who are engaged in farming only is preserved at BGN 50. The new point in the social security legislation is that in 2004 tobacco growers will be in the same privileged position.

**With the approved 2004 SSS Budget the 2004 maximum pension amount was fixed at BGN 420** (or 35 per cent of the maximum income for social security purposes, as proposed by the financial ministry). The opinion of NSSI's experts that it is inadmissible to eliminate since 2004 the provision for limiting pensions up to a certain amount before the necessary financial stability is in place and before starting to apply the reformed legislation on a new sound basis prevailed. **The maximum amount of the unemployment benefit is increased from BGN 70 to BGN 80, and the maternity benefit for raising children up to 2 years of age is increased from BGN 110 to BGN 120**.

According to the approved 2004 SSS Budget, **insured persons will be entitled to pregnancy and childbirth benefits, if they have 6 months length of service for social security purposes**, of which 3 months within a year before the month of the pregnancy and childbirth leave. Besides, the persons must be insured against all social risks except accident at work or occupational illness, or against all social risks except unemployment. Legally regulated length of service for social security purposes did not exist before. To receive pregnancy and childbirth benefits, the insured person was required to have not less than one week length of service. **Insured persons must satisfy the same requirements for the length**



**of service for social security purposes to get entitled to benefits for raising small children.** The new stricter conditions for pregnancy and childbirth benefits and for the benefits for raising small children set different legal requirements for the minimum length of service for social security purposes which gives the right to benefits for temporary disability as a result of general illness and to benefits for pregnancy, childbirth and raising small children. There is a need to make uniform the legal requirements for these risks.

**The lower contribution to the Pension Fund for persons born after 31 December 1959, decreased from 27 to 26 per cent owing to the higher contribution to universal pension funds, increased by 1 percentage point since 1 January 2004, i.e. from 2 to 3 per cent,** is a highly motivating factor for involvement of young people in the social security system. Directing more social security assets to the private universal pension funds where they get invested and generate income for the insured person, enables the young people to get in the future higher pension income guaranteeing higher living standards.

*Guarantees for the claims of workers and employees in the event of employer's bankruptcy*

In November 2003 the Government approved the draft law on the guaranteed claims of workers and employees in the event of employer's bankruptcy. According to this draft law the claims of workers and employees will be guaranteed with calculated but unpaid labor remunerations, as well as with pecuniary damages for employer's account established by a regulation or a collective labor contract in the event of employer's bankruptcy. The draft law developed by MLSP is in accordance with the requirements of Council Directive 80/987/EEC concerning the approximation of Member States' legislation on the protection of workers and employees in the event of employer's bankruptcy.

**According to the draft law, a Fund for Guaranteed Claims of Workers and Employees in the Event of Employer's Bankruptcy will be set up within NSSI;** it will have an independent budget and independent management with prevailing employers' participation. Revenues in the fund are expected to come from: mandatory monthly contributions by employers to the amount of up to 0.5 per cent of the income for social security purposes; revenues from entry into the rights of creditors in bankruptcy procedures; income from investment of temporary idle cash assets of the fund; temporary financial aid and grants, and other sources.

The objective is to have employers' contributions accumulated in 2004, which will allow to cover the guaranteed claims payment costs since 2005. The draft law also fixes a maximum amount of guaranteed claims depending on the duration of the worker's or employee's labor relation and depending on whether it exists as at the moment in which the right of guaranteed claims

originates. If the contributions in this new fund are not made at the expense of the contributions in the SSS Unemployment Fund, then the law formally suggests introduction of additional social security burden for employers.

*New ordinances of the Financial Supervision Commission*

**Four new ordinances of FSC** on the activity of pension insurance companies and the pension funds they manage, as well as on the interests of the insured persons in such PFs were promulgated in the Official Gazette in the last quarter of 2003. These include:

- Ordinance No. 3/24.09.2003 on the terms and procedure of changing the participation or transferring the accumulated funds of an insured person from one supplementary pension insurance fund to another corresponding fund managed by another pension insurance company;
- Ordinance No. 9/19.11.2003 on the terms and procedure of valuation of the assets and liabilities of supplementary pension insurance funds and of the pension insurance company, of fund's net assets value, on the calculation and announcement of the value of one share, and on the requirements for keeping individual lots;
- Ordinance No. 10/26.11.2003 on the requirements for the composition and the structure of the equity capital (capital base) of the pension insurance company and for the minimum liquid assets of the company and the supplementary pension insurance funds managed by the company;
- Ordinance No. 12/10.12.2003 on the terms and procedure of determining the minimum yield in managing the assets of the supplementary mandatory pension insurance funds, of covering the gap to the minimum yield and on the formation and use of reserves to guarantee the minimum yield.

FSC's Ordinance No. 3, which regulated the disputable points in changing the participation or transferring the accumulated funds of an insured person from one pension fund to another, was widely discussed in the public space. The role of the insurance broker in changing the pension fund was dropped in the final text of the ordinance. **Since 2004 a new fund will be chosen in person or by proxy. The application to change the pension fund will be filed with the pension insurance company managing the fund to which the insured person wants to get transferred.** The relationship of insured persons with the previous pension funds will only be terminated upon signing the new insurance contracts.

**The participation in a supplementary pension insurance fund may only be changed** and the funds accumulated in the individual lot may only be transferred to another corresponding fund managed by another pension insurance company **upon elapse of two years from signing the first insurance**

**contract or from the date of official assignment after the insurance obligation has originated.** Outside this case, the participation in a supplementary pension insurance fund may be changed after elapse of one year from signing the insurance contract with the fund. The assets accumulated in individual lots may be transferred from one supplementary pension insurance fund to another one managed by another pension insurance company not more than once in a calendar year. The objective of the limitation on the frequency of changing the pension fund is to enable efficient management of accumulated insurance assets and to guarantee higher yield on invested assets for the insured persons.

The time period for transfer of insured persons from one pension fund to another will be different, depending on when the insured person decides to change the pension fund and on whether the question is about change of a supplementary mandatory or supplementary voluntary pension fund. **Where a supplementary mandatory pension fund is changed, the pension insurance companies will only transfer the accumulated insurance assets on four dates throughout the year (15 May, 15 August, 15 November, and 15 February),** depending on the quarter in which the persons have filed their application for transfer. Therefore, **the change of a pension fund will take the least time if the insured person states his choice at the end of a quarter and the most time when the application is filed in the beginning of a quarter.** As regards voluntary pension insurance funds, pension insurance companies transfer the assets in the individual lots on the 15th day of the month following the month in which the transfer procedure has begun. The objective of this difference in the time periods for transfer of the insurance assets between the supplementary mandatory and the supplementary voluntary funds is to guarantee to the maximum the interests of the persons insured for a second pension. **Transfer will not be possible before the corresponding fund reports its yield. That will allow the insured persons to compare alone the yields achieved by the different pension insurance companies and to take objective decisions about the future management of their insurance assets.**

**The specific amount of the transfer charge** is fixed in the rules on the structure and procedure of supplementary mandatory or supplementary voluntary pension insurance funds and this amount **may not exceed BGN 20.** If the tax is not paid within the stipulated time limit, the ordinance entitles pension insurance companies to deduct the amount due from the assets in the individual lots.

**Experts expect that not more than 5-10 per cent of the insured persons will change their pension fund.** The campaign will allow smaller pension insurance companies to increase their market share, which may well make them aggressive in attracting new members.

## *New Social Security and Labor Migration Regulation Agreements*

In the fourth quarter of 2003 **Bulgaria signed a Social Security Agreement and an Administrative Agreement on its Implementation with Serbia and Montenegro, as well as a Labor Migration Regulation Agreement with Spain and an Administrative Agreement on Implementation of the Social Security Treaty signed with Spain on 13 May 2002. The Government also approved an Agreement on the Export of Social Security Payments with the Kingdom of the Netherlands.** That put the start of the cooperation between Bulgaria and the Netherlands, which implies signing a bilateral agreement for full coordination in the social security area at a later stage.

By signing new social security agreements, Bulgaria made an important step towards higher coordination of the national social security system with the systems operational in the EU Member States and the candidate countries, which is a requirement of the European legislation. The synchronization of the social security systems of these countries will undoubtedly guarantee higher social protection of workers and will encourage the free movement of workers within the EU, which is a precondition for improved competitiveness of the European economy as a whole and for attaining the 2000 Lisbon criteria.

## *Supplementary Pension Insurance*

The data about insured persons, assets, and investments of pension funds, presented in the tables and figures below enable to analyze the development of Bulgaria's supplementary pension insurance, with focus on the last quarter of 2003. It should be pointed out that the information about voluntary pension funds is as of 30 November 2003, whereas the data about the other funds (universal and occupational) are as of 31 December 2003.

Data about the insured persons and the available net assets in pension funds reveal that in the fourth quarter of 2003 **the number of insured persons and the available net assets in UPFs have registered the highest growth (+6.29 per cent and +22.91 per cent, accordingly)** compared to the other supplementary pension insurance funds.

With the increase of the social security contribution to UPF from 2 to 3 per cent in 2004, UPFs are expected to accumulate a higher amount of assets, which should be reasonably invested in different financial instruments. **For a year the number of insured persons in all pension funds has increased by 26.80 per cent,** with the number of insured persons in UPFs registering the highest growth - 38.59 per cent accordingly. **For a year the net assets in pension funds have increased by 49.71 per cent,** with UPFs registering again the highest growth in their assets - 173.49 per cent.



The established permanent upward trend of the relative share of assets in UPFs in the aggregate pension assets (registering an increase from 21 per cent at the end of the third quarter to 23 per cent at year end) at the expense of the relative share of assets in VPFs (dropping down from 50 per cent at the end of the third quarter to 48 per cent at year end) was preserved in the fourth quarter as well, which is mainly a result of the growing number of insured persons in UPFs

As at end of 2003 PIC Doverie AD has managed to attract the highest total number of insured persons for the three types of funds (42.14 per cent). This company accounts for the highest share of insured persons in OPFs and UPFs – 42.38 per cent and 47.07 per cent accordingly, giving in to no one but PIC Allianz Bulgaria AD on the number of insured persons in VPFs. In terms of the market share regarding pension assets PIC Doverie AD is again second after PIC Allianz Bulgaria AD. PIC Doverie AD holds 32.16 per cent of pension assets, whereas PIC Allianz Bulgaria AD holds 38.41 per cent.

The tendency to have pension fund assets invested predominantly in government-issued or government-guaranteed securities and in national bank deposits was preserved in the last quarter of 2003, but a growing diversification of funds' portfolios is observed. Considerable increase in the share of investments in mortgage bonds is observed, particularly for universal and occupational funds, mostly at the expense of the share of investments in government-issued or government-guaranteed securities and the share of investments in securities accepted for trading at the regulated securities market. The share of investments in foreign securities remains all but unchanged, which is a result of both the high as yet legal limitations on UPFs' and OPFs' investments abroad and the lack of investment experience in the pension funds.

In 2004 pension companies are expected to focus their efforts on enhancing the efficiency of their investment activity, on improving the quality and efficiency in servicing the insured persons, on updating their information systems, and on improving the qualification of the staff of pension companies. Through the so-called "accounting shares" to be introduced since 1 July 2004 the insured persons will have daily information about the condition of pension funds and the achieved yield on investment of the insurance assets accumulated in the individual lots. With that end in view, the companies should develop their own rules for daily valuation of assets. The process of building the secondary legislation base is expected to get completed with the approval of the ordinances on the activity of custodian banks, on investments abroad, and on actuary licensing.

According to the 2004 projections of the Bulgarian Association of Supplementary Pension Insurance Companies (BASPIC), total assets accumulated in

supplementary pension insurance funds (universal, occupational and voluntary) will reach BGN 685 m. To achieve this goal, the companies should improve the efficiency of their investment activity to guarantee higher yield for the insured persons and expand the scope of the insured persons in the three types of investment funds.

## Supplementary Pension Insurance

Table 9. Insured Persons in Pension Funds

	As of 31.12.2002	As of 30.09.2003	As of 31.12.2003	Share of insured persons by funds as of 31.12.2003, in %	Variation against 30.09.2003, in %	Variation against 31.12.2002, in %
Total insured persons in supplementary pension insurance funds	1804469	2 177 470	2 288 011	100.00	5.08	26.80
Total insured persons in UPFs	1 164 482	1 518 408	1 613 875	70.54	6.29	38.59
Total insured persons in OPFs	155 196	161 901	164 943	7.21	1.88	6.28
Total insured persons in VPFs*	484 791	497 161	509 193	22.25	2.42	5.03

\*Information about VPFs is as of 30 November 2003  
Source: Social Security Supervision Department, FSC, as well as own estimates

Table 10. Available Net Assets of Pension Funds

	As of 31.12.2002	As of 30.09.2003	As of 31.12.2003	Share of pension assets by funds as of 31.12.2003, in %	Variation against 30.09.2003, in %	Variation against 31.12.2002, in %
Total available net assets in supplementary pension insurance funds, thousand BGN	332465	453 525	497 744	100.00	+9.75	+49.71
Available net assets in UPFs, thousand BGN	41705	93 652	114 058	22.91	+21.79	+173.49
Available net assets in OPFs, thousand BGN	95241	131 449	143 816	28.89	+9.41	+51.00
Available net assets in VPFs*, thousand BGN	195519	228 424	239870	48.19	+5.01	+22.68

\*Information about VPFs is as of 30 November 2003  
Source: Social Security Supervision Department, FSC, as well as own estimates

Table 11. Market Shares of Pension Insurance Companies as at end of 2003

Pension insurance company	Market share, in %				
	By number of insured persons in VPFs *	By number of insured persons in OPFs	By number of insured persons in UPFs	By total number of insured persons*	By net assets amount*
PIC Doverie AD	26,42	42,38	47,07	42,14	32,16
PIC Saglasie AD	6,48	18,60	12,16	11,36	10,08
PIC DSK-Rodina AD	4,30	3,98	5,75	5,30	4,77
PIC Allianz Bulgaria AD	49,73	22,13	19,92	26,71	38,41
PIC I N G AD	3,77	3,71	8,78	7,30	6,10
PISC CKB-Sila AD	3,23	3,82	3,09	3,17	1,95
PIC LUKoil Garant – Bulgaria AD	6,07	5,39	3,24	4,02	6,53
Total	100,00	100,00	100,00	100,00	100,00

\*Information about VPFs is as of 30 November 2003

Source: Social Security Supervision Department, FSC, as well as own estimates

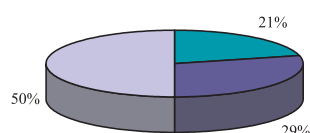
Table 12. Pension Funds' Investments in Different Financial Instruments

Investments in	Total for UPFs as of 30.09.2003	Total for UPFs as of 31.12.2003	Total for OPFs as of 30.09.2003	Total for OPFs as of 31.12.2003	Total for VPFs as of 30.09.2003	Total for VPFs as of 30.11.2003
Government issued or government guaranteed securities	77,78	71,68	70,99	68,97	55,29	58,57
Total securities accepted for trading at regulated securities markets	8,8	3,84	10,71	6,57	9,33	7,89
Mortgage bonds	0,00	10,87	0,00	7,10	9,44	8,56
Municipal bonds	0,42	0,23	0,60	0,50	0,59	0,42
Bank deposits	13,45	13,15	16,89	16,12	20,79	20,51
Investment estates	0,26	0,22	0,77	0,72	3,51	3,29
Investments abroad	0,01	0,01	0,02	0,02	0,03	0,01
Other investments	0,00	0,00	0,00	0,00	1,01	0,75
Total	100,00	100,00	100,00	100,00	100	100

Source: Social Security Supervision Department, FSC, as well as own estimates

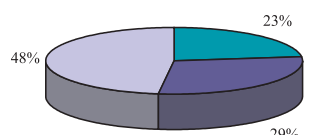
Figure 11. Relative share of pension assets by funds

As of 30 September 2003



Net assets of UPFs	Net assets of OPFs	Net assets of VPFs
--------------------	--------------------	--------------------

As of 31 December 2003\*



Net assets of UPFs	Net assets of OPFs	Net assets of VPFs
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\*Information about VPFs is as of 30 November 2003

Source: Social Security Supervision Department, FSC, as well as own estimates

## Health Reform

### 2004 National Framework Agreement

NHIF, BDU and UDB declared willingness to have the 2004 National Framework Agreement signed on time and taking effect without delay as of 1 January 2004, but unfortunately that did not come true. On one hand, because the Ministry of Health was late in developing the basic documents regulating the parameters of the negotiations between NHIF, BDU and UDB so as to eliminate any regulatory barriers to the signing of NFA 2004. On the other hand, the serious split of opinion between the doctors and the national health insurance fund on the new mechanisms to finance medical institutions proposed by NHIF and MoH revealed that **the tendency of National Framework Agreements taking effect with delay will be preserved.**

MoH did not present **the four new ordinances regulating the basic implementation principles of the national health policy in 2004** until the end of December 2003. These documents defined the scope of the health insured persons, their rights, and the national health policy parameters. The objective of the amendments is to balance better the interests of health insured persons and medical care contractors, to improve the quality of medical services and the procedure for access of health insured persons to medical services, but only time will show whether that will be achieved. The four new documents developed by MoH include:

- Ordinance No. 25/23.10.2003 on determining the list of illnesses for which treatment at home shall be fully or partially payable by the National Health Insurance Fund
- Ordinance No. 28/25.11.2003 on preventive and clinical examination
- Ordinance No. 29/12.12.2003 on determining the basic package of health activities guaranteed from NHIF's budget
- Ordinance on the access of health insured persons to the medical institutions for outpatient and hospital care

**The amendments to Ordinance No. 25 correct technical, legal and medical inaccuracies and wordings** and according to MoH they do not limit patients' rights and do not narrow the scope of illnesses for which NHIF pays the medicines for home treatment.

**A new approach was applied in developing Ordinance No. 28.** This ordinance regulates the illnesses for which patients are subject to clinical examination and the procedure of the preventive and clinical examination provided by medical and health institutions. The volume, frequency of examination and payment of clinical examination activities should be determined in the negotiations between NHIF, BDU and UDB. The advantages of the ordinance include clear and precise specification and expanded scope of the illnesses, with guaranteed equality of all patients with chronic illnesses. At the request of pregnant women, preventive examinations will be carried out by an obstetrician or by a general practitioner. Children up to 2 years of age will have the right to monthly examinations for control of their development by outpatient care pediatricians. The idea is to guarantee higher quality of medical services.

Ordinance No. 29 determines the basic package of health activities guaranteed from NHIF's budget. **The 2004 basic hospital care package includes 111 clinical paths covering a total of 1950 diagnoses.** There are no significant changes in the basic package for primary outpatient medical care. The scope of highly specialized activities, which may be carried out within the primary and hospital care, is given in greater detail for the specialized outpatient care. Some of the highly specialized activities formerly carried out within the specialized outpatient care are transferred to hospital care medical institutions with a view to improve the quality of services for hospital care patients. **The new point in the ordinance is the guaranteed minimum of examinations, consultations and tests for the clinical examination, which are payable by NHIF. A new point is also the introduction of a package of activities for medical consultations, tests and documents required for labor-and-medical examination, with a view to improve the access of patients to the Medical Commissions of Labor Experts.**

The amendments to the Ordinance on the access of health insured persons to outpatient and hospital care medical institutions are associated with the **eliminated zoning of medical institutions since 1 January 2004**, regulated in the Health Insurance Act. The patients' choice of a medical institution and the workload of hospitals will be indicators of the quality of medical care. Hence the serious concerns of doctors and trade unions about the liquidation of small municipal hospitals because patients do not prefer them. It is true that Bulgarian medical institutions do not make full use of their capacity, which leads to their inefficient operation. In 2004 the free choice of medical institutions by patients will show how to optimize the Bulgarian system of medical institutions.

**According to data from the health insurance fund, 229 000 people changed their general practitioner in December 2003**, which reveals that now health insured persons invoke in full their right to change their general practitioner when they are not satisfied with the quality of medical care. Major reasons to change the general practitioner include in the first place the violated access to specialized care and the quality of medical services. The free choice of a general practitioner in 2003 created conditions for intensified competition of doctors, which guaranteed higher quality of the primary outpatient medical care. The free choice of a medical institution in 2004 is expected to create conditions for intensified competition of medical institutions, which will guarantee higher quality of hospital medical care.

**The new mechanism of financing medical institutions proposed by NHIF and MoH generated serious discord between the doctors and the health insurance fund.** The approved Act on the 2004 State Budget of the Republic of Bulgaria envisages that in 2004 the Ministry of Health shall subsidize hospital care medical institutions with state and municipal interest in their capital on the basis of annual contracts for work according to a uniform methodology. **Total BGN 280 m are planned in MoH's 2004 budget to finance all hospitals with state and municipal interest in their capital for the activities, which are not covered by clinical paths.** MoH will pay for these activities on a "price of diagnosis" basis.

**The Bulgarian Association of Private Medical Institutions also objected to the new hospital financing conditions.** At the end of November it sent an official declaration to the Parliamentary Health Commission, the Ministry of Health, the Management Board of NHIF, the MB of BDU and the MB of UDB. According to the Association of Private Medical Institutions (APMI) the proposed financing mechanism for medical institutions will place state, municipal and private medical institutions under dissimilar conditions. APMI proposed to have legislative changes made, which will guarantee equal financing treatment of medical institutions irrespective of the

type of their ownership. The Association's idea is to enable health insured persons to make the difference and not to pay in full for their treatment in a private medical institution where they can get medical services of higher quality. An equal treatment of state, municipal and private medical institutions would obviously be in the interest of health insured persons.

**For the first time medical institutions start the new year with minimum debts.** That was made possible because at the end of December the Government allocated additional funds of BGN 31 m from the 2003 central budget to MoH's budget. **Thereby the 2003 total additional subsidies for medical institutions amounted to about BGN 120 m**, of which BGN 15 m were allocated for capital expenditures. **In 2004 the Ministry of Health is expected to make activity-related pay to all state and municipal hospitals – 67 with state interest in their capital and 109 with municipal interest.** As MoH did not manage to develop in the last quarter of 2003 the procedure of subsidizing hospitals with state and municipal interest in their capital, **the plan for the first three months of 2004 is to finance each hospital with 1/12 of the 2003 annual subsidy.** Equalization and payment according to new prices for the patient flow in the first quarter of 2004 will be made after the operating account reports of hospitals on the activity till 25 April 2004 are prepared.

The new points in the 2004 NFA are expected to include **full electronic carrier reporting of medical care contractors**, which aims at improving the control in the health care system and at optimizing its activity. General practitioners and hospitals will start reporting on electronic carriers since 1 July 2004, and medical care contractors in special outpatient care medical institutions must do that till 31 December 2004.

The absence of an information system is among the reasons for the inefficient performance of Bulgaria's medical institutions. **MoH's initiative to start building a national hospital information system in 2004** with a view to improve the control of clinical paths, to optimize hospitals' performance and capacity, and last but not the least, to provide patients with medical services of higher quality can be given a positive assessment.

## Medicines Policy

The first Bulgarian positive list of medicines, specified by MoH, generated tension among foreign pharmaceutical producers and research pharmaceutical producers. On 10 December 2003 the Minister of Health presented the positive list of medicines developed by a commission of 13 members. **The first Bulgarian positive list of medicines, which is a basic implementation instrument of the national health policy, includes 2477 medicinal products united in 667 international non-patented names.** It covers 87 per cent of the medicines for which the producing companies have

filed applications with the commission. According to the health minister, the positive list of medicines includes all 1423 medicines currently payable by NHIF in full or in part and it takes account of the public interest to provide quality and effective medicines to a maximum number of people.

**The basic criteria of placing medicinal products on the positive list of medicines include: quality, efficiency, safety and pharmaco-economic analysis.** Only 5 medicines, which are unique and have no alternative, are placed on the list. About 75 per cent of the medicines on the list are generic medicines. The other medicines are interchangeable in the treatment of an illness.

The fact that a large portion of the medicines of foreign pharmaceutical producers are not placed on the positive list of medicines made the Bulgarian Association of Research Pharmaceutical Producers and the US Association of Pharmaceutical Producers to send an official open letter to the Council of Ministers of the Republic of Bulgaria concerning the development of the positive list of medicines on 8 December 2003. According to the representatives of the above organizations, the positive list of medicines in this restrictive form will deprive Bulgarian patients of "modern, high quality and efficient treatment with medicines used all over the world, which have been offered in Bulgaria for years." What is more, they believe that the positive list of medicines in its current form is expected to lower the investment interest towards the Bulgarian market and to impede the process of Bulgaria's accession to the EU.

**The discontent of foreign pharmaceutical producers is mainly a result of the expected lower sales of their products in 2004.** It should be pointed out that according to data from the Executive Agency for Medicines (EAM) the Bulgarian pharmaceutical market amounts to about BGN 622 m, registering an increase of BGN 66 m compared to 2002. The share of Bulgarian sales in money terms is about BGN 211 m, and that of foreign medicines – about BGN 411 m. For comparison, in 2002 sales of Bulgarian pharmaceutical producers amounted to over BGN 196 m, and the turnover of foreign companies amounted to about BGN 360 m. The slight decrease in the share of the sales of Bulgarian medicines in 2003 (from 35 per cent in 2002 to about 34 per cent in 2003) is a result of the introduced good management practice (GMP) rules, which caused companies to close some of their production shops. **The basic problem related to the positive list of medicines and concerning the interests of Bulgarian and foreign pharmaceutical producers is to determine which interests – of the generic or of the original industry – are more consistent with the public interest of the State.**

**MoH's initiative to organize in 2004 a public discussion for optimization of the medicines regulatory system is**



given a positive assessment. According to the currently effective regulation, the positive list of medicines is published once in a year. **The plan is to discuss the idea of publishing the list of medicines twice in a year and to have the commission engaged in its development institutionalized and operational year-round.** Thereby MoH aims at making the medicinal policy more dynamic and flexible. The plan is also to expand the scope of the positive list of medicines to cover the medicines payable in full or in part by NHIF as well as all medicines payable from the state budget via the Ministry of Health, the Ministry of Defense and by the hospital care medical institutions. The trend of developing Bulgaria's pharmaceutical market regulation in accordance with the experience of the other European countries targets future integration of the positive list of medicines and the reimbursement list of NHIF and having them developed by a single body.

**The invitation to involve Bulgarian experts in the work of the standing commissions and the work groups at the European Drugs Agency** before Bulgaria's full EU membership is an exceptional recognition of Bulgaria's achievements in the pharmacy area, of the successfully completed negotiations between Bulgaria and the European Commission on the pharmaceutical legislation and of the compliance of the national legislation and practice with the so-called *acquis communautaire*.

## Health Insurance Payments from NHIF

The table below presents the growth against 2003 of the funds for health insurance payments planned in NHIF's 2004 budget. Calculations reveal that the amount planned in NHIF's 2004 budget for **health insurance payments of medicines for home treatment registers the highest growth (increasing by 45.3 per cent in 2004 against 2003)**. Funds for dental aid and for hospital medical care register the second highest growth by 23.1 per cent and 22.6 per cent accordingly, which is explainable by the Government-declared willingness to continue the reform in the hospital sector.

The amount of about BGN 162 m planned for medicines in NHIF's 2003 budget was unrealistic, given the reported 2001 and 2002 expenditure of BGN 182 m and BGN 239 m accordingly. Despite the higher amount for medicines planned for 2004 and the measures to stabilize monthly medicines expenditure at BGN 19-20 m, it is important to point out that due to the absence of an information system within the health care sector the funds for medicines may well prove insufficient in 2004 as well.

Table 13. Health Insurance Payments from NHIF's Budget in 2003 and 2004

	NHIF's Budget, 2003	Updated NHIF's Budget, 2003	NHIF's Budget, 2004	Growth 2004/2003, %	Growth 2004/Updated budget 2003, %
Health insurance payments (BGN):	627 753 000	676 105 000	769 705 200	22,6	13,8
For primary outpatient medical care	103 500 000	103 500 000	103 500 000	0	0
For specialized outpatient medical care	82 400 000	82 400 000	94 000 000	14,1	14,1
For dental medical care	39 800 000	39 800 000	49 000 000	23,1	23,1
For medical diagnostics activity	39 300 000	39 300 000	41 000 000	4,3	4,3
For medicines for home treatment	162 753 000	211 105 000	236 500 000	45,3	12,0
For hospital medical care	200 000 000	200 000 000	245 105 200	22,6	22,6

Source: Act on the 2003 Budget of NHIF (promulgated, Official Gazette No. 119/27 December 2002), Act on the 2003 Budget of NHIF (promulgated, Official Gazette, as amended, No. 107/9 December 2003) and Act on the 2004 Budget of NHIF (promulgated, Official Gazette No. 114/30 December 2002)

## Other Legislative Initiatives

At the end of 2003 major legislative initiatives in the health care sector included the passed Act on Blood, Blood Donation and Blood Transfusion and the Supplemental Act to the Health Insurance Act.

The passed **Act on Blood, Blood Donation and Blood Transfusion**, which repealed the previous Act on Blood Donation and Blood Transfusion, introduced for the first time measures to control the quality and safety of blood and blood components. **The Act specified with precision and clarity the principles** to be observed in carrying out the activities regulated therein, such as: voluntariness and gratuitousness in the donation of blood and blood components; protection of the rights and health of donors and recipients; equality of donors and recipients; rational use of blood and blood components, and last but not the least, blood and blood components self-sufficiency of the country. **The act treats in a modern way the promotion of blood donation**, integrating in this activity the Ministry of Health, the Bulgarian Red Cross, the transfusion chemotherapy centers, hospital care medical institutions, non-government organizations and religious communities.

The objective of this act is to improve the condition of blood donation in Bulgaria, which has been assessed by experts as extremely alarming in the recent 10 years. The average number



of blood donors in Bulgaria is 18 per 1000 people, in some regions this number is below 10 persons per 1000 people. The World Health Organization recommends 50 blood donors per 1000 people.

**The Supplemental Act to the Health Insurance Act**, passed by the National Assembly on 20 December 2003, solved the problems of persons who owe more than three health insurance payments for themselves and/or for members of their families for the period 2000 - 31 December 2003. By the end of March 2004 they are to file with the regional offices of NSSI requests to be allowed to pay by installments till 31 December 2004 their health insurance debts with principal amount exceeding BGN 50. It should be pointed out that these persons will lose their health insurance rights if they fail to pay their obligations until the deadline of rescheduling and if they fail to make more than three health insurance payments due for 2004, with the effect of rescheduling also terminated in the second case.

## Regulatory Framework

In the fourth quarter of 2003 government administration continued regulating environmental policy on waste management – an environmental sector directly related to the conditions and results from enterprises' activity.

Following the adoption of the Waste Management Act in September, at the end of 2003 a **National Program for Waste Management Activities** was published, aimed to analyse the condition of the sector and organize the future actions of the central and local authorities for the period until 2007. The Program presents a sufficiently clear picture of the problems and existing practices of current waste management. A major reason for the poor condition of the sector is the lack of reliable information on the quantities and the morphological composition of industrial and municipal waste on the basis of which efficient management decisions should be formulated. As particularly acute is identified the lack of methodology for objective calculation of the quantities of generated waste at storage, a lack of activities for separate collection of waste, sorting, recycling and disposal of waste as well as the great number - 4 584 of unregulated dung-hills and municipal waste-polluted sites. In spite of the efforts of the government administration which worked out a register and a detailed plan for a step-by-step closing of unregulated dung-hills, the problem of organized waste collection and treatment of polluted sites will remain in the short run one of the most serious financial and organizational challenges faced by local authorities. The areas identified as most polluted are Stara Zagora, Sofia and Varna and the reason for this type of pollution are the industrial enterprises operating on the territory of these cities. Huge industrial waste generators in the country are the power plants in the Maritsa – Iztok, Kremikovtsi AD of Sofia, Yumikor Med AD of Pirdop, Stomana Industry AD of Pernik, Agropolichim AD of Devnia, Solvey Sodi AD of Devnia.

A key task of the National Program for Waste Management is to propose a system of measures to allow, in the context of expected growth in industrial output for the period until 2007, the quantity of generated waste to GDP to be stabilized at the levels of 2001<sup>9</sup>. The government announced that BGN 835 m is needed to finance the activities under the Program. So far foreign donors have financed most of the activities and now the administration is faced with the task of finding efficient regulatory mechanisms which will allow more active involvement of additional sources of financing, including private capital. A model for achieving the projected results is sought through an attempt at **reassessment of the economic instruments used for stimulating waste prevention, rational management and use**.

<sup>9</sup> For 2001 generated waste totaled 91 156 thousand tons, including harmless industrial waste of 86 397 thousand tons and municipal waste of 4 003 thousand tons.

<sup>10</sup> National Program for Waste Management Activities, [www.moesw.government.bg](http://www.moesw.government.bg).

**Municipal waste charges** currently set in proportion to the tax assessment of the property owned cannot stimulate reduction of waste quantity and introduction of practices for separate collection. The practice of recent years of increasing the funds paid to municipal budgets by raising the garbage fee did not lead to the intended higher quality of the services for garbage collection, transportation or cleaning of the communities. The existing difference in the basis for charging municipal waste for natural persons and companies additionally inhibits introduction of stimuli for activities related to waste sorting and preliminary treatment. Therefore raising of the municipal waste charge proposed in the National Program could be viewed as a "passive measure" rather than a realistic evaluation of the role of this financial instrument in environment protection policy.

The Program envisages two additional options for tax preferences for the activities related to prevention and reduction of the quantity of waste:

- **exemption from VAT of transactions related to waste collection and transportation, separate collection, waste use and treatment**, for cleaning and rehabilitation of unregulated depots and waste-polluted areas;
- **remission, exemption or reduction of profit tax for companies investing in recycling of municipal, industrial and hazardous waste**.<sup>10</sup>

Without a specific proposal for the scope of the above-mentioned tax preferences and their connection with the second program principle, according to which "increasing waste management costs should play the role of a stimulus for reducing the quantity of generated waste," it is difficult to give an objective assessment of the economic effect from the impact of the proposed financial mechanisms. Obviously the same economic instruments cannot be employed at the beginning of the process and at the end of the program period, 2007, when Bulgaria must prove results in the waste management area comparable to the general practice of EU member states. The issue of the specific actions of the administration on the application of the whole set of regulatory measures in the sector (the Waste Management Act, the National Program and additional provisions) currently remains open, given the fact that most of the envisaged measures come into force in early 2004 under financial conditions already stipulated by the State Budget Act for 2004.

In October 2003 Bulgaria ratified the international **Convention on Access to Information, Public Participation in Decision-making and Access to Justice in Environmental Matters (known as the Aarhus Convention)**. The Convention is perceived as setting a new model of relations at international, national and local levels, related to public participation in decision-making and access to justice in environmental matters. Its objective is that individuals, nongovernmental organizations and the public should play a more significant role in the formulation and implementation of environmental

protection policy and that individuals should be completely informed on a timely basis about the quality of their living environment. Its application should lead to a more profound accounting of the environmental considerations in developing and implementation of sector policies, strategies, action plans, programs and projects, in the context of sustainable development and environmental protection and improvement.

## Environmental Practices

Following the deal with the hydro plant "Tsankov Kamak", **Overgas Inc AD is the second Bulgarian company to finance its projects by selling carbon credits in accordance with the regulations of the Kyoto Protocol ratified by Bulgaria.** According to the joint project between the Dutch government and the company an investment plan for EUR 1.5 m has been developed for the gasification of Veliko Tarnovo, Gorna Oriahovitsa and Liaskovets (including 40 industrial consumers, over 80 public buildings and about 16 000 households) and renovation of the fuel installations in the three areas. As a result of the project greenhouse gases will be reduced by some 350 thousand tons. The project envisages, after completion of the construction of the gasification network at the end of 2007, the company to start selling the rights to carbon dioxide emissions to the Dutch government in accordance with the conditions of the scheme for purchase-sale of units of reduced emissions ERUPT 3. As a result of the project at the end of 2007 the company will be capable of providing the whole amount of carbon credits for the planned period 2008 – 2012 and according to estimates it may generate additional revenues (besides those from the sale of natural gas) in the amount of 20-25 per cent of the initial investment.

## Financing of Environmental Activities

In November 2003 **financing of an investment project amounting to EUR 1.125 m on the water cycle of Sofia** and a waste water treatment plant in Kubratovo was approved. The financing is in form of grant under ISPA European Program and accounts for 75 per cent of the total value necessary for project implementation, the remaining portion under the project to be co-financed from the state budget. Preparation of the project will start in July 2004 and construction in September 2006. Thanks to this project the share of the citizens of Sofia whose waste water is subject to full treatment is expected to increase to 60 per cent, the number of the population serviced by the sewerage system will increase and damming of waste water in the open water streams in the city will decrease.

**The European Bank for Reconstruction and Development announced in December 2003 the launch of a loan for infrastructure investment in the environmental area earmarked for renovation of the water supply companies in the country.** The first loan to be granted by the Bank without government guarantees is for six water supply companies in the

amount of EUR 20 m. The total amount of the loan is EUR 60 m for 15 years and three-year grace period and the companies that have received funds under it will apply for additional co-financing of the projects under EU ISPA Program.

The World Bank grants a USD 300 000 aid for the setting up of a **Bulgarian Energy Efficiency Fund**, which will credit projects on restricting air pollution and enhancing energy efficiency. The Fund is expected to receive the first financing from the Global Environmental Fund (GEF) in the amount of USD 10 m for energy-saving projects restricting air pollution. The Fund will generate additional environmental benefits to Bulgaria, as its aim is to reduce carbon dioxide emissions. Estimates show that in the first ten years of its operation it will be able to support the financing of projects totaling over USD 80 m.

**A biodiversity component under the project entitled Bulgaria – Development of the Forestry Sector**, financed with a World Bank loan, will be set up within the structures of the already existing National Trust Eco-Fund. The funds under this component are in the form of aid of USD 7 m for 6 years – a grant by the GEF. The Fund will ensure support for infrastructure development and other capital investments, park management and implementation of projects in tourism, as well as other programs for development of protected territories. Within the framework of the biodiversity component under the project for development of the forestry sector USD 700 000 are allocated for target conservation programs. These funds will be utilized by park directorates for recovery and protection of habitats and populations of rare species. Over USD 400 000 are envisaged for small grant programs for local communities and NGOs to integrate conservation objectives in forestry management. In May 2004 the documents under the project will be submitted for consideration to the Board of the World Bank. If approved, the project will start to be implemented in the fall of 2004. The Bulgaria – Development of the Forestry Sector project will be implemented in two phases – preparatory and investment. The preparatory phase involves profound studies of the conservation, use, protection and management of forestry resources and substantiation of major project forecasts by component and financial support, to be implemented in the investment phase. The objective of the project in the preparatory phase is to set the basic parameters for optimizing the value of forestry resources and implementation of a sustainable model of Bulgarian forestry sector management through:

- improving the management of the public forestry sector;
- enhancing the capacity for management of private and municipal owners of forests;
- enhancing the carbon benefits from the Bulgarian forests;
- adapting government management of forests to the market economy and the new circumstances resulting from the restitution.

**The Loan in Support of Environment and Privatization**

granted to Bulgaria by the World Bank will be extended with six months. The EPSAL loan is a structural loan amounting to USD 49.5 m, made in three tranches in support of harmonizing the Bulgarian environmental legislation with the *acquis communautaire*. The third tranche of EUR 20 m was made in end-December 2003. The project supports the pilot introduction of integrated permits for protection against pollution in accordance with Directive 91/96 on integrated pollution control. Beneficiaries are Bulgarian companies implementing programs for removal of old environmental damages – Agropolichim AD of Devnia, Geosol AD of Provadia, Pirel AD of Gotse Delchev, Neochim AD of Dimitrovgrad, Biovet AD of Peshtera, KTSM AD of Plovdiv, Osogovo AD of Kyustendil, and OTSK AD of Kardjali. Beneficiaries are also pilot programs for bringing the activity in conformity with the environmental legislation, implemented by the following companies: Yumikor AD of Pirdop, Chimko AD of Vratsa and Sviloza AD of Svishtov.

The greater part of financial intermediation in Bulgaria passes through the banking system. Although credit expansion continued, the condition of banks in Bulgaria continues to be stable with excellent indicators of capital adequacy and liquidity and well-functioning bank supervision. However, growth in receivables from loans to the non-government sector slowed somewhat in the fourth quarter probably due to the restrictive bank supervision measures taken or announced in the last months of the year. The year ended with 35 banks in Bulgaria (following the licensing of the new West-East Bank AD in the summer), including 29 banks licensed to perform transactions in the country and abroad and six branches of foreign banks.

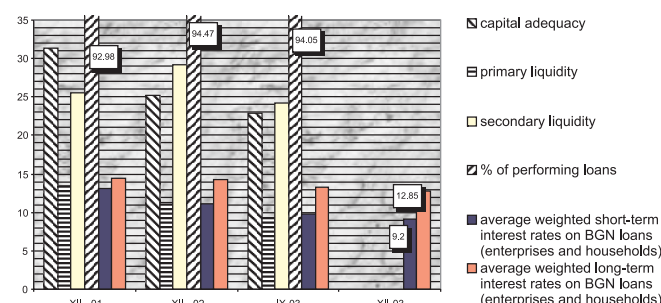
## Statistics of the banking system

As of 1 January 2003 International Accounting Standards became effective for commercial banks in Bulgaria which entailed a **change in the format and structure of their balance sheets and income statements**.

As of April the Banking Supervision Department of the **BNB modified the grouping of commercial banks** (as before, with the special note that grouping does not contain any elements of rating and should not be interpreted as an assessment of the financial condition of the banks). A bank's position in the groups depends on the size of its assets. Group One always comprises 10 banks, Group Two - the remaining ones, and Group Three consists of the branches of foreign banks in Bulgaria.

According to BNB data, at the end of 2003 the banking system has assets at the amount of BGN 17 323 643 thousand while at the end of September these were BGN 16 386 230 thousand (an increase of BGN 937 413 thousand in the fourth quarter). At the end of the year deposits amounted to BGN 13 593 516 thousand while at the end of September these were BGN 12 690 460 thousand (an increase of BGN 903 056 thousand in the fourth quarter). In December the current profit of the banking system was BGN 379 817 thousand while in September it was BGN 293 663 thousand. According to the latest available data from the BNB, the total capital adequacy of the banking system at the end of September 2003 was 22.97 per cent (excluding Group Three) against 23.87 per cent three months earlier (25.22 and 31.32 per cent at the end of 2002 and 2001 respectively). At the end of September 2003 the total primary liquidity of the banking system was 9.3 per cent, and the secondary liquidity was 24.3 per cent (respective indicators three months earlier were 9.77 and 25.98 per cent, at the end of 2002 - 11.2 and 29.25 per cent respectively, and at the end of 2001 - 13.47 and 25.47 per cent). Some of these indicators are shown in Figure 12.

Figure 12. Selected indicators of the banking system (%)



Source: according to BNB data, monthly information bulletins

**Thus, the banking system generally continued to increase its assets, deposits and current profit in the fourth quarter. However, growth in assets is lower than that in the third quarter while growth in deposits exceeds that in the third quarter. This is due in part to the slowdown in credit growth.** The current profit of the banking system at the end of the year exceeds current profits in the last two years. The net interest income/other non-interest income ratio is preserved at high levels despite the insignificant drop over the quarter (from 2.30 and 2.25 at the end of 2001 and 2002 respectively it reaches 2.30 at the end of September and at the end of 2003 it is 2.21). This indicates that lending remains a primary source of income for the banks in Bulgaria, at the same time suggesting underdevelopment and inadequate diversification. Capital adequacy and liquidity indicators at the end of September are lower than those at end-June but they are relatively very high, a sign of the stability of the banking system. This confirms the conclusion that **the Bulgarian banking system is stable but there is unutilized capacity for development and improvement of its efficiency.**

The above conclusion is also indirectly confirmed by the comparison of Bulgarian banks' credit exposure with other transition economies. Despite credit growth in the recent years Bulgaria still lags behind most Central and Eastern European countries, though the region as a whole is still far behind the indicators of the developed market economies (Table 14). This is indicative of existing potential for credit expansion to the private sector in Bulgaria, regardless of the disputes about its optimum rate. At the end of 2003 banking system receivables on loans to private enterprises and households account for 25.6 per cent of the updated forecast<sup>11</sup> for annual GDP.

<sup>11</sup> According to MoF data, Government Debt monthly bulletin, December 2003.



Table 14. Lending in Central and Eastern Europe  
(at the end of 2002)

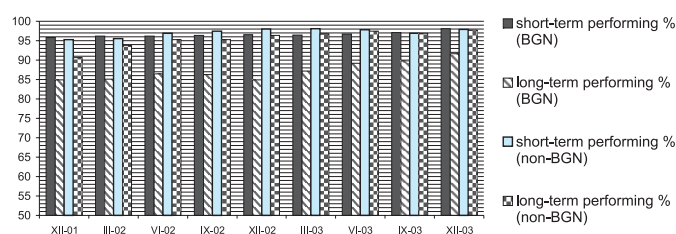
Country	Domestic lending to private sector * against GDP, %
Bulgaria	18.0
Estonia	29.8
Lithuania	14.2
Poland	15.2
Romania	8.4
Russia	17.3
Slovak Republic	25.2
Slovenia	41.0
Hungary	34.0
Croatia	45.0
Czech Republic	20.0

\* Loans to private enterprises and consumer loans.  
Source: EBRD, Transition Report 2003

**Lending to the non-government sector confirms the upward trend** (under the Currency Board arrangements these are the loans from commercial banks including loans to non-financial state-owned enterprises, private companies, households and non-banking financial institutions). From BGN 4374627 thousand at the end of 2001, receivables on loans to the non-government sector reached BGN 6 250 741 thousand at the end of December 2002. At the end of December 2003 receivables on loans to the non-government sector reached BGN 9 303 120 thousand, i.e. **the annual growth in receivables on loans to the non-government sector accounts for 48.8 per cent.**

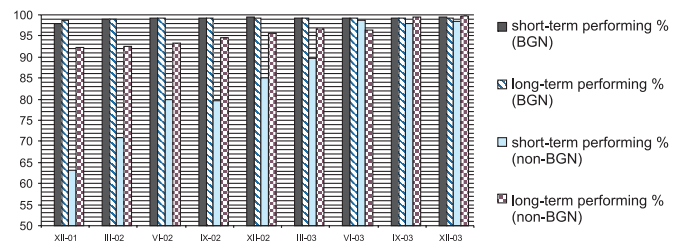
Newly contracted loans from commercial banks for 2002 totaled BGN 5 189.7 m while for 2003 newly contracted loans amounted to a total of BGN 7 159.96 m (**annual growth rate of 38 per cent**). **The condition of the loan portfolio is good** – 94.47 per cent were classified as performing loans in all categories of loans in the banking system at the end of 2002, while at the end of September 2003 performing loans accounted for 94.05 per cent (Figure 12). The general conclusion about the condition of the loan portfolio applies in particular to receivables on loans to private enterprises and households – the percentage of performing loans increased or remained high in the fourth quarter of 2003 (Figures 13 and 14).

Figure 13. Condition of the loan portfolio: private enterprises (revised data after December 2002)



Source: BNB data, monetary report, and own calculations

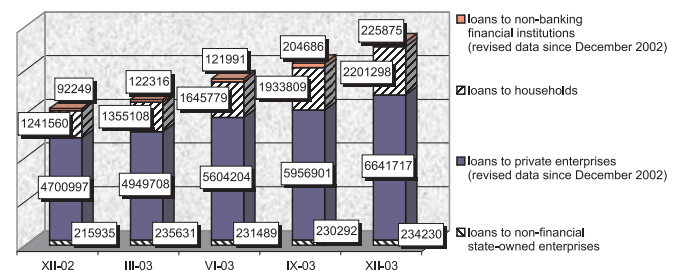
Figure 14. Condition of the loan portfolio: households (revised data after December 2002)



Source: BNB data, monetary report and own calculations

**Interest rates on short-term and long-term loans in BGN in December are lower than those in September** (Figure 12). The dynamics of loans reveals even more interesting short-term trends (according to currency, term and borrowers). Thus, for instance, the review of receivables on loans to the non-government sector in the fourth quarter illustrates a most sizeable growth in lending exposure to private enterprises and households but their relative share in total receivables remains almost unchanged (Figure 15).

Figure 15. Receivables on loans to the non-government sector (BGN thousand)



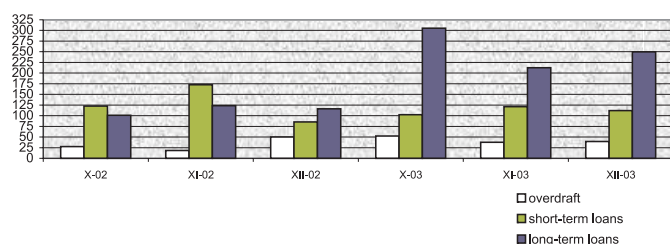
Source: BNB data, monthly information bulletins

Figures 16, 17, and 18 present the dynamics of newly contracted loans for 2002 and 2003. The last quarter of 2003 shows increased lending activity compared to the same period of 2002. As regards terms and currency, **generally the trend of higher growth of long-term versus short-term loans in BGN and Euro is preserved**. However, in the fourth quarter long-term loans in USD prevail over short-term ones but their growth on the same period of 2002 is insignificant. Overall (total short-term and long-term loans), compared with the same period of previous year, of note is the lower volume of newly contracted loans in USD against serious growth in loans in BGN and Euro. All this is a manifestation not so much of interest rates dynamics or interest rate levels but rather of increased investment activity in the country, taking account of the currency risk. Short-term expectations for the dynamics of the USD exchange rate to the Euro seem to be contradictory and thus neutral in respect of the currency choice when applying for loans. However, the presence of currency risk (for the Euro as reserve currency in the

## BANKING SYSTEM

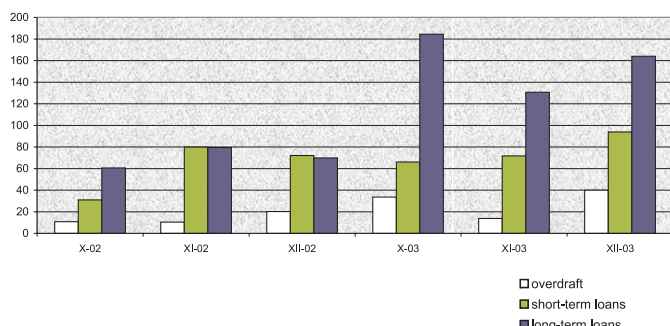
conditions of the Currency Board Arrangement) predetermine preferences to loans in BGN and Euro.

Figure 16. Newly contracted loans from commercial banks in BGN (BGN m)



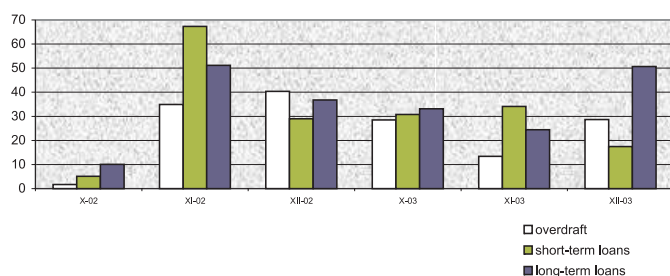
Source: BNB data, monthly information bulletins

Figure 17. Newly contracted loans from commercial banks in EUR (BGN m)



Source: BNB data, monthly information bulletins

Figure 18. Newly contracted loans from commercial banks in USD (BGN m)



Source: BNB data, monthly information bulletins

The total credit growth and in particular the higher volume of long-term loans in the last two years are offset by some changes in the structure of bank assets and liabilities. According to the analytical reporting of commercial banks, the volume and share of foreign assets decreased most noticeably, while the volume and share of some long-term liabilities grew most significantly (Table 15).

Table 15. Changes in the structure of some assets and liabilities

	XII-01	VI-02	XII-02	VI-03	IX-03	XII-03
Foreign assets, BGN thousand	4665301	3689571	3803121	3250586	3520629	3002680
Share of foreign assets in total assets, %	36.30	28.44	25.09	20.29	20.61	16.59
BGN time deposits over 2 years, BGN thousand	12278	45464	73794	98442	104838	117320
BGN time deposits over 2 years, share in total liabilities, %	0.10	0.35	0.49	0.61	0.61	0.65
Forex time deposits over 2 years, BGN thousand	2184	3950	19539	45599	56531	81595
Forex time deposits over 2 years, share in total liabilities %	0.02	0.03	0.13	0.28	0.33	0.45
Debt securities over 2 years, thousands of BGN	6341	11666	15962	42834	44849	53981
Debt securities over 2 years, share in total liabilities, %	0.05	0.09	0.11	0.27	0.26	0.30
Foreign liabilities	696801	630400	893617	959799	1173162	1498366
Foreign liabilities, share in total liabilities, %	5.42	4.86	5.90	5.99	6.87	8.28
Capital and reserves	1637348	1688445	1921575	2106270	2152455	2270309
Capital and reserves, share in total liabilities, %	12.74	13.02	12.68	13.14	12.60	12.54

Source: BNB data, analytical reporting of commercial banks

The table shows that **despite banks' enhanced efforts to attract more long-term deposits and issue longer-term debt securities on the domestic capital market, capital, reserves and foreign liabilities preserve the most significant relative weight in the structure of liabilities.**

### Restructuring and other events in the banking system

Through various channels like privatization, opening of representation offices, branches and newly established banks **foreign participation in the banking system of Bulgaria is already predominant both with regard to control over equity and managed assets.** At the end of 2002 private persons owned 83.4 per cent of the total assets of the banking system. At the same time foreign banks and investors controlled 72 per cent of banking assets.<sup>12</sup>

In 2003 the last large state-owned bank was DSK Bank AD which together with Encouragement Bank accounted for the last 14.2 per cent of the state-owned share in banking assets

<sup>12</sup> BNB Annual Report 2002.

(the municipal share is 2.4 per cent). **The privatization of DSK Bank** began as early as mid-2002 with the selection of privatization consultants and in May 2003 the Bulgarian Consolidation Company (BCC) selected the Hungarian OTP as the preferred buyer of DSK Bank. Little after that the contract was signed under which the buyer had to deposit EUR 31.1 m to the account of BCC (or 10 per cent of the offered price for DSK Bank). The remaining amount was to be remitted after the transfer of the shares in favor of OTP.

A 90-day period followed during which the Hungarian institution had to obtain the required permits from supervisory authorities and from anti-monopoly regulators of both countries. The time limit expired on 26 September. The last permit (from BNB) was obtained at the end of September after the Hungarian bank provided the requested additional information on the shareholders' equity and the equity structure of the bank (from Hungarian side information was requested in relation to the media reports of suspected OTP participation in a financial scandal in Hungary). The deal was finalized at the beginning of the fourth quarter with simultaneous order of the remaining portion of the remittance and transfer of the shares by BCC to the buyer. OTP expressed their intention to invest BGN 600 m over the next five years, to complete DSK Bank's restructuring, to improve its information technology and upgrade its branch network.

**With this deal bank privatization in Bulgaria is officially completed. After the sale of DSK Bank AD more than 97 per cent of the total banking system assets are held by private persons and foreign banks and investors control over 85 per cent of bank assets<sup>13</sup>.** Encouragement Bank AD and Municipal Bank AD are the last banks with state, respectively municipal, control on the equity capital.

The delayed **appointment of a new governor and a deputy governor (Head of Issue Department) of BNB** continued till the beginning of the fourth quarter. Although the term of office of the current governor expired in June and the deputy governor (and head of the Issue Department) resigned as early as the beginning of the year the National Assembly elected a new governor and a deputy governor as late as October. This was a key issue for the banking system during the year and most of the discussions and assessments of the experts focused on the independence of the BNB, the political considerations of the choice, including the BNB role in the management of the fiscal reserves.

During the quarter the discussion about the possible **threats consistent with the intensified lending activity of the banks** continued. The quality of loan portfolios and the potential stability of the banking system were in the center of the discussion but (mainly after the visit of the regular mission of the IMF to Bulgaria) the experts and those responsible for economic policy decision-making began to discuss also the relationship

between growing imports, the current account deficit and credit expansion. The IMF representatives insistently argued about the necessity of even stricter control over banks' lending activity.

In spite of the general understanding of the benefits from credit growth for overall economic growth as well as the lack of immediate threats for the stability of the banking system, the BNB adopted the IMF arguments about the necessity to reduce growth in lending to private enterprises and households. The measures taken in this regard include firstly **the amendment to Regulation No. 9 of the BNB** (Regulation No. 9 on the valuation and classification of risk exposures of banks and the formation of provisions for devaluation losses) of August 2003. The term by which a loan exposure starts to be deemed doubtful (91 to 120-day past due payments) or a loss (already over 120-day past-due payments) has been shortened by two months with the amendment. In early 2004 Regulation No. 9 was amended again and the risk exposures were classified into four, instead of five classification groups (the former groups "doubtful" and "loss" are combined into "non-serviced" - for over 90-day past-due payments).

The latest IMF report on the review of the stand-by agreement with Bulgaria highlighted **another three steps taken by the Bulgarian authorities, aimed at cooling down the credit expansion**. Firstly, BNB postponed its plan for reducing minimum reserve requirements of banks. Secondly, the announced intention of the government<sup>14</sup> to take back the deposited funds (in mid-2003) from the fiscal reserve with the commercial banks when deposits mature or earlier. The government took commitment not to repeat such operations in 2004 with the argument that depositing part of the fiscal reserve with commercial banks creates conditions for additional credit expansion. Thirdly, the BNB confirmed its support to the joint project with the Association of Commercial Banks to launch by mid-2004 the operation of the single credit register, which will cover credits of less than BGN 10 thousand as well (representing the current minimum amount of credits, separately and together, of individual borrowers and related persons, about which the BNB maintains a credit register). With the registration of all credits it is expected that banks' costs for creditworthiness evaluation, monitoring the credit portfolio and risk management in general will be reduced. To this end Regulation No. 22 on the Central Credit Register is to be amended.

In early 2004 the Bulgarian authorities announced before the IMF<sup>15</sup> **the expectation that real annual growth rate in receivables from the non-government sector will be reduced below 25 per cent at the end of 2004.**

<sup>13</sup> The calculations are against the assets at the end of 2002.

<sup>14</sup> Additional memorandum on the economic policy of BNB and the government, 15 January 2004.

<sup>15</sup> Ibidem.

Major events to the operation of the banking system in the fourth quarter were the **adoption of the new Regulation No. 10 on the Internal Control in Banks as well entry into force in the beginning of November of new General Conditions of cash service of BNB customers with banknotes and coins in the form of valuable parcels.**

Another commented event of the last months was the procedure for the **privatization of the national card operator Borica AD.** Initially (in August 2003) the BNB selected an appraiser of Borica AD and subsequently the criteria for the selection of a buyer were to be adopted. The news about the possible sale attracted the attention of a number of financial institutions in the country as well as potential foreign investors. Toward the beginning of the fourth quarter there was no specific development on the privatization but the main discussed options involved the sale of the card operator to Bankservice AD or simultaneous acquisition of interest by all banks with a specific form of mediation by the Association of Commercial Banks. Both options are based on the necessity to maintain competitiveness and efficiency of service.

The continuing uncertainty in combination with the interest in the future of Borica provoked additional discussions and in early 2004 the Association of Commercial Banks put forth a proposal to the BNB to assign to the manager of the company to work out a medium-term strategy for its development with the participation of an independent consultant. A key element of this strategy should be the scheme for the sale of Borica. Inasmuch as assessment of the fair interest of each bank in the card operator is an issue of primary importance, the Association proposed the following criteria – number of cards issued, number of automatic teller machines or effected settlements. The argument is that most active institutions on the card market will get due interest in the operator.



A successful year for the development of the Bulgarian capital market ended with the fourth quarter, although the upward trend in some market indicators halted namely in this quarter. During the fourth quarter stock exchange trading was active, with growing turnover in the stock and bond markets and a slight fall in the market for compensatory instruments. The SOFIX index was increasing through most of the period, hitting all-time high values, despite some partial loss of value in the second half of the period. Market capitalization grew further in this quarter. Turnover and trade volume exceeded those in the third quarter (not taking into account the sale through the stock exchange of the state-owned blocks, e.g. those of DZI AD in the third quarter, Zlatni Piasatsi AD in the fourth quarter and Oil and Gas Exploration and Extraction AD in the third and fourth quarters).

**Yet, the role of the capital market in the financial sector of Bulgaria is still insignificant** – as of the end of 2003 total market capitalization of the Bulgarian Stock Exchange – Sofia AD comprised 7.89 per cent of the revised GDP forecast<sup>16</sup> for 2003. The Bulgarian capital market is still an unpopular channel of financial intermediation and this conclusion remains valid even in comparison with Central and Eastern European countries – by the share of market capitalization to GDP Bulgaria ranks last after Romania and the eight Eastern European countries joining the EU in 2004<sup>17</sup>. By absolute value of market capitalization Bulgaria is lagging considerably too (Table 16). The state of the capital market is consistent with the prospects of the Bulgarian economy as a whole, and the circumstance that financing mechanisms via such an alternative non-banking environment remain unknown or non-preferred even with available relevant projects. **Liquidity is growing higher but generally stays low, market incentives are insufficient to establish good practices of corporate governance even in some public companies. Investment alternatives remain limited and financial intermediation is still provided mainly through the banking sector.**

Table 16. Market capitalization in EU and Central and Eastern European countries (EUR b)\*

Eurozone (12), total	3826.0
EU (15), total	6060.1
Newly accessing countries to the EU (10), total	80.3
Bulgaria	1.4
Estonia	2.8
Cyprus	3.8
Latvia	0.9
Lithuania	4.1
Malta	1.5
Poland	27.0
Slovak Republic	2.7
Slovenia	5.5
Hungary	12.7
Czech Republic	19.3

\* Data on Bulgaria are as of end-December and on the remaining countries, as of November 2003.

Source: Eurostat, Bulgarian Stock Exchange – Sofia AD

### The capital market through the indicators of the Bulgarian Stock Exchange – Sofia AD (excl. the market for compensatory instruments and investment vouchers)

As of 31 December 2003 market capitalization based on stock exchange data amounted to a total of BGN 2 722 008 207 (out of these BGN 985 984 573 on the Official market) while at the end of the third quarter market capitalization amounted to a total of BGN 2 426 253 973 (out of these BGN 474 620 504 on the Official market). Listing of new companies for trade on the market segments of the Official market (transfer of the issue of Petrol AD on the official market) also contributed to the double quarterly growth in market capitalization on the Official market. Turnover in the fourth quarter of 2003 was BGN 147 502 533 with 22 369 904 traded securities. The turnover and volume of trade do not include the privatization market (e.g. the sale of the residual state interest in Zlatni Piasatsi AD and Oil and Gas Exploration and Extraction AD), nor the compensatory instruments and rights traded on the exchange and investment vouchers traded for the first time on the stock exchange. However, block deals are included in the turnover and volume (again without compensatory instruments and investment vouchers). This reflects higher turnover and volume compared to the previous quarter. The SOFIX index rose to reach another record high since the start of its calculation on 10 November – 456.34 (exceeded later in early 2004). The index closed the year with a value of 454.34 (against 413.26 at the end of September 2003 and 183.08 at the end of December 2002).

Thus, **the fourth quarter of the year was marked by a positive development of the major indicators characterizing the condition of the Bulgarian capital market** (understood and measured traditionally through the indicators of the Bulgarian Stock Exchange – Sofia AD). Excluding privatization, compensatory instruments and investment vouchers but including block deals, the exchange turnover and the volume of trade increased in this quarter (the volume and turnover increased even if the results from privatization in the two quarters are added). Market capitalization and the SOFIX index exceeded their end-of-September values (total capitalization – by 12 per cent, and the index – by 10 per cent).

**Low liquidity remains a major problem, irrespective of the positive trends in recent quarters.** For instance, in December half of total turnover on the Official stock market was generated by eight deals in shares by one company (Bentonit AD). The number of issues registered for trading continues to be high but liquid positions are few (these are most of the securities included in the SOFIX index plus some of the former privatization funds).

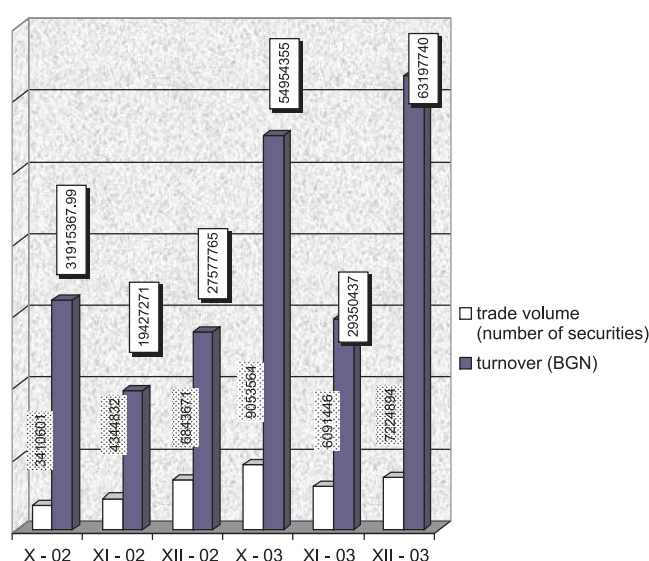
<sup>16</sup> According to MoF data, Government Debt monthly bulletin, December 2003.

<sup>17</sup> According to EBRD data, Transition Report 2003.



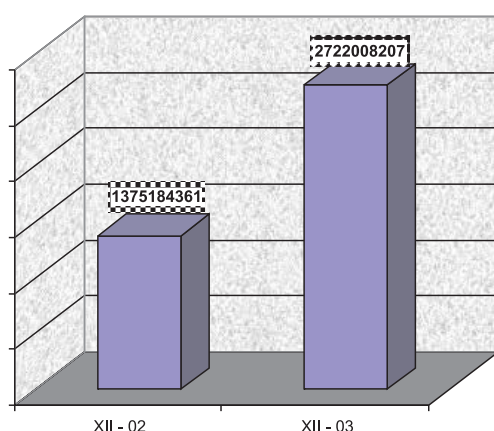
The positive development is confirmed by comparisons with the corresponding period of 2002 (even without the privatization market, the markets for compensatory instruments and investment vouchers). With regard to volume, trade on the Bulgarian Stock Exchange – Sofia AD in the fourth quarter of 2003 exceeded considerably (by 53 per cent in total for the three months) the same period of the previous year. Quarterly turnover also marked a significant growth (by 87 per cent in total for the three months) on an annual basis (Figure 19). Market capitalization grew by 98 per cent on an annual basis (Figure 20).

Figure 19. Trading on the Bulgarian Stock Exchange – Sofia AD (fourth quarters of 2002 and 2003, excluding privatization market and markets for compensatory instruments and investment vouchers)



Source: According to data from the Bulgarian Stock Exchange – Sofia AD, monthly bulletins

Figure 20. Total capitalization of the markets on the Bulgarian Stock Exchange – Sofia AD at the end of period (BGN)



Source: According to data from the Bulgarian Stock Exchange – Sofia AD, monthly bulletins

During the fourth quarter the financial statements of public companies for the first nine months of 2003 were to be published. The impression from the previous year that market participants need and already take into account fundamental factors affecting the price of shares (particularly the financial information from the reports and news from the traded companies) was confirmed. The price dynamics of shares, especially on liquid positions, reflects to greater extent corporate events, which is a sign of **better investment culture of market participants and improved market efficiency** as a whole.

Like in previous reporting periods many of the companies did not submit their statements in time. This in turn confirmed another observation related to the Bulgarian capital market – **corporate governance practices in Bulgaria need improvement** and often even public companies do not take into account the importance of corporate governance in favor of minority shareholders and potential investors.

In the fourth quarter **there was certain revival of the bond market** on the Bulgarian Stock Exchange – Sofia AD. A total of 79 deals of corporate bonds were concluded in the fourth quarter on the Official market of the Bulgarian Stock Exchange – Sofia AD, the same number as in the third quarter but with a total turnover of BGN 16.7 m (against BGN 4.5 m in the third quarter). Corporate bonds deals on the Unofficial markets of the stock exchange totaled 75 (against 67 in the third quarter) with a total turnover of BGN 13.6 m (against BGN 7.5 m in the third quarter).

In the fourth quarter the mortgage bonds of First Investment Bank AD (second mortgage bond issue of this bank) and the corporate bonds of Alma Tour BG AD (first issue of the company) and of Kaolin AD (second issue of the company) were registered for secondary trading on the stock exchange. All the three issues had been privately placed and fully executed before that. In the fourth quarter the FSC recorded in its registers two more issues of corporate bonds – those of Raiffeisenbank EAD (three-year, amounting to USD 32 104 000) and TBI Credit EAD (three-year, amounting to BGN 8 m).

**Private placement and subsequent registration on the stock exchange is the preferred strategy by issuers** with the purpose of lowering the risk of placement failure while ensuring higher liquidity for investors. In confirmation to this we can point out that no transactions in bonds were concluded on the primary market of the stock exchange during the quarter. It is quite probable that some of the privately placed issues will soon join the above three issues registered for secondary trading on the Bulgarian Stock Exchange – Sofia AD and the issues registered by the FSC. It should be noted that most of the issues are mortgage bonds of banks, which is undoubtedly

related to the increased demand for mortgage loans in recent months.

In the fourth quarter of 2003 **the shares of yet another open-ended investment company, TBI Eurobond AD**, which was granted a license for conducting transactions by the FSC in the previous quarter **were registered for trading on the stock exchange**. This increased the number of open-ended investment companies traded on the Bulgarian Stock Exchange – Sofia AD to three. **The shares of Bulgarian Information Technologies AD were also registered for trading** on the stock exchange in the last quarter. The registration provoked interest for two reasons. Firstly, this is the first Bulgarian hi-tech company with public status traded on the stock exchange. Secondly, inasmuch as the shares were registered for trading straight on the Official market, in compliance with the requirement of the rules for trading<sup>18</sup> in early December the Board of Directors of the stock exchange adopted new special rules for primary sale of shares upon registration on the Official market. The first transactions under the new rules set a precedent for such cases of registration.

In October the **Bulgarian Stock Exchange – Sofia AD changed the list of issues used for calculation of the SOFIX index**. The issues are 13 instead of 10 after adding new companies with good liquidity – Orgachim AD, DZI AD and Central and Cooperative Bank. According to the opinions of analysts and professional participants in the market, the exchange index becomes a little more representative with the inclusion (for the first time) of a bank and an insurance company.

#### **Trade in compensatory instruments and investment vouchers, stock exchange privatization**

**The start of compensatory instruments trading on the Bulgarian Stock Exchange – Sofia AD in 2002 remained among the leading events** in the area of the capital market throughout 2003. The initial positive expectations of investors and participants in privatization against compensatory instruments resulted in initial price rise of the securities and later on in continuous preservation of prices at levels close to one fourth of the nominal value. Interest in compensatory instruments trade is comparable to that in shares trading but it depends directly on the progress of privatization through the stock exchange (especially the sale of larger blocks of more attractive companies) where payment is to be effected in compensatory instruments.

After the positive news about compensatory instruments trading on the Bulgarian Stock Exchange – Sofia AD in mid-

year gave way to disclosures about **so-called problem lots** (which still are or have been subject to litigation with regard to the lawfulness of their issue, already used in privatization transactions) the decision of the Supreme Administrative Court in June confirming the revocation of compensatory warrants of a nominal value of BGN 142 m accelerated **amendments to the Act on Compensatory Instruments Transactions**. According to the statutory amendments, “problem lots” not registered in the Central Depository shall be blocked in the Central Register of Compensatory Instruments. If already registered in the Central Depository, blocking shall be done there; however, the instruments that have been subject of a transaction on the regulated market are not subject to blocking (these are acquired by a third person in good faith like the acquirers of compensatory instruments on the stock exchange). Such instruments cannot be invalidated and in the case when a court makes a determination that they were issued without legal grounds or on legal grounds repealed subsequently, a person who has enriched himself without such grounds by their issue shall return the same quantity and nominal value of compensatory instruments.

All these changes in the Act on Compensatory Instruments Transactions, though somewhat delayed, aimed at regaining certainty among participants in the capital and privatization market. Another major amendment to the Act on Compensatory Instruments Transactions in 2003 **provided for a possibility for the Bulgarian Stock Exchange – Sofia AD to hold technically (after assignment under a contract from the Privatization Agency) centralized public tenders for sale of shares owned by the state and municipalities as well as public tenders for sale of interest in limited liability companies owned by the state and municipalities**. The new possibility was related mainly to the privatization of non-public companies but nevertheless it could enhance indirectly interest in the markets of the Bulgarian Stock Exchange – Sofia AD. The change confirmed the positive assessment and credibility of the trading and settlement systems already available on the Bulgarian capital market.

In spite of the changes in the Act on Compensatory Instruments Transactions aimed at solving the cases with the “problem lots” and transferring execution of the tenders to the stock exchange, compared with the previous quarter compensatory instruments trading statistics reported a decline. **The decline in secondary trade in non-cash instruments of payment is a fact, even if investment vouchers traded in the fourth quarter of 2003 for the first time on the Bulgarian Stock Exchange – Sofia AD** are added to the volume and turnover.

In November the Board of Directors of the stock exchange adopted changes to the rules of trading (specifically amending Appendix No. 6 adding investment vouchers to compensatory instruments). After approval of the changes by the FSC in the second half of November 134 132 876 investment vouchers of

<sup>18</sup> When the issue is registered straight on an Official bourse segment, without having been traded on other segments, the requirements for free float are deemed to be fulfilled if a specific per cent of the issue is offered for sale through an irrevocable instruction submitted by one or more of the existing shareholders to a member of the stock exchange. After that the issue is subject to a six-month period of monitoring (under Art. 54, para. 4 of the stock exchange rules).

BGN 1 nominal value were registered. The first stock exchange transactions in this instrument were closed on 24 November 2003. Initially there was great interest and transactions were effected at 17 per cent of the nominal value but by the end of November their price decreased.

The main reason for the lower prices of vouchers compared with compensatory instruments is their limited application in privatization as well as the fact that their validity expires in mid-2004. With a view to expanding the opportunities for the sale of investment vouchers in January 2004 the PA and the stock exchange started applying in practice for the first time the trading system of the Bulgarian Stock Exchange – Sofia AD<sup>19</sup> for conducting the first two tenders for sale of stock and shares against which investment vouchers could be used. At one tender shares of 432 companies were offered (stock exchange segment “Centralized Public Tender”) and at the other one – LTD-company shares in 86 companies (stock exchange segment “Non-attendance Public Tender”). At these tenders payment could be effected in investment vouchers as well as in cash and compensatory instruments.

**Trading statistics of compensatory instruments and investment vouchers** for the period October – December 2003 is as follows: a total of 5 562 deals with compensatory instruments were concluded (versus 4 986 in the third quarter) with a turnover of BGN 16 267 416 (versus BGN 21 522 377 in the third quarter). The data include both compensatory instruments and investment vouchers. In addition, however, block transactions with compensatory instruments and investment vouchers were registered on the stock exchange – 19 deals with a total turnover of BGN 2 972 864, a decrease on the previous quarter. During the quarter compensatory instruments were traded at a price of 20.91 to 24 per cent of the nominal value, at lower average prices compared with the third quarter. Investment bills in the quarter hit a bottom low of 13.05 per cent of their nominal value and a maximum high of 18.09 per cent of the nominal value.

Among the major events in the area of bourse privatization in the fourth quarter was the sale on the privatization market of the residual interest of 51 per cent in **Oil and Gas Exploration and Extraction EAD** following the sale completed earlier in September for the initial 49 per cent. The residual package was sold as one indivisible lot of the privatization segment against cash payment. Thus Oil and Gas Exploration and Extraction EAD proved to be one of the few companies privatized fully through the Bulgarian Stock Exchange – Sofia AD. Although the value of the shares of the company traded on the secondary market fell following the completion of the privatization of the company, interest in sales was highlighted

as another example of the benefits of public offering through the stock exchange as a privatization method and as a good example of government support for the development of the capital market in the country.

Another event was the sale of the residual state interest (11.24 per cent) in **Zlatni Piasatsi AD**. In October and November on the privatization segment for payment in compensatory instruments, at three stages, the shares were sold off and the average price exceeded considerably the initially announced minimum price in compensatory instruments. During the privatization tenders for Zlatni Piasatsi AD investor interest led to parallel rise in the prices of shares in the “normal” lev market of secondary trading and in the prices of compensatory instruments traded. Thus not only participants in the privatization but also secondary market speculators were able to generate profits.

Another major event in the privatization was the sale for the first time on the Bulgarian Stock Exchange – Sofia AD of the **companies from the energy sector** – major interests in Energoremont Holding of Sofia and three of its subsidiaries (in Ruse, Varna and Bobovdol) were sold. In the fourth quarter the residual minority interest in **IPK Rodina AD** was offered for sale through the stock exchange.

**Thus the year 2003 proved to be the most successful one for the stock exchange privatization so far.** The strong growth, respectively the potential of the exchange mechanism to conclude efficiently privatization deals in the future, are confirmed by the annual data. For 2003 (respectively 2002) 155 (61) deals were effected on the privatization market in BGN, with turnover of BGN 16 490 690 (BGN 2 886 742). For 2003 (respectively 2002) 2 108 (33) deals were closed on the privatization market with compensatory instruments (and investment vouchers in 2003), with turnover of BGN 284 063 012 (BGN 309 013).

### **Regulatory environment and decisions of the Financial Supervision Commission**

Following major **changes in the regulation of the capital market** in the third quarter (Regulation on the Requirements to the Activity of Investment Intermediaries and a new Regulation on the Prospectuses for Public Offering of Securities and Disclosure of Information by Public Companies and Other Issuers of Securities, adopted by the Financial Supervision Commission) in the fourth quarter of 2003 the **FSC adopted several new (replacing fully the existing analogous) regulations**. This is the Regulation on the capital adequacy and liquidity of investment intermediaries, the Regulation on the licenses for conducting transactions as a stock exchange, an organizer of unofficial securities market, an investment intermediary, a managed company and a company with special investment purpose, the Regulation on the Central Depository

<sup>19</sup> This was made possible after the Board of Directors of the stock exchange adopted a new Appendix No. 8 to the Rules, establishing the terms and procedure for execution of so-called non-attendance public tenders for sale of shares in limited liability companies owned by the state and municipalities. Again for the purpose of execution of tenders assigned under contract by the AP for sale of shares in state and municipally-owned companies, in the beginning of October the Board of Directors of the stock exchange adopted an Appendix No. 9 to the Rules, establishing the terms and procedure for so-called centralized public tenders.

of Securities, as well as the Regulation on tender offering for purchase and exchange of shares.

It should be noted that in the fourth quarter the **FSC issued a new license for conducting transactions as an open-ended investment company** (to Advance Invest AD), whereby already four open-ended investment companies (excluding the Pioneer Investment Management SA registered in Luxembourg) and two close-ended companies operate on the market. Emergence of companies for management of investment portfolios of institutional and professional investors reflects the growing interest in the opportunities for investment returns offered by the Bulgarian capital (and financial) market. On the other hand, interest may be provoked by the prospects for attracting the increased funds of households and enterprises and their channeling into investments outside the country.



Two events of significant importance for the energy sector occurred in the past quarter. The Energy Act was finally passed almost at the same time with the official start of the privatisation of EDCs. The signed Memorandum of Understanding on the Regional Energy Market in Southeast Europe and its Integration into the European Community Internal Energy Market was a step forward towards the establishment of a regional energy market. The building contract for the Tzankov Kamuk HPP and dam-lake was signed. International oil quotations registered an increase. The trend was accompanied by an increase of oil product excise duties in Bulgaria.

## Government Policy

**The long-awaited Energy Act was passed in the last quarter of 2003.** The draft law was developed as early as the beginning of 2003, but was not put for second reading in Parliament until the end of November. With the official passing of the EA the reforms targeting introduction of competitive principles of operation in the energy sector continued. The change of the regulatory framework governing the relations in the sector is a serious precondition both for the sector's further development on national level and for its integration in the single European energy market.

The Act regulates all relations in carrying out the activities in the electricity industry and the heat and gas supply sectors, as well as the role of government bodies in determining the national energy policy, the regulation and the control in the energy sector. The Act also covers the issues of electricity production from renewable energy sources (RES).

**The EA contains a couple of new points regarding the state regulation in the sector.** The current powers of SERC are enriched by new ones. The Commission will issue certificates of origin of the electricity, as well as green certificates, to the producers of electricity and heat from RES and according to combined methods. The new Act also amends SERC's modes of financing. Further to its capacity of a primary authorizing institution of budgetary funds, SERC will also finance its activity from the fees collected for treatment of applications, issuance of certificates, sale of tender documents, as well as from the license fees. Twenty per cent of the fines and penalty payments, as well as donations, will form the balance of the Commission's budget revenues. The above amendments further guarantee the Commission's financial independence, which is a precondition for higher quality of its activity. On one hand, because SERC becomes less dependable on the State, and on the other hand, because of the opportunity to finance from these revenues the costs of improving the qualification of the employees in the administration of the regulatory body. The higher revenue flows provide opportunities to increase the analyses and examination costs and the material resources development costs. It is very important for the electricity consumer protection to clearly define the Commission as a body, which shall treat complaints

against irregularities in the licensing activities – an issue, which was not regulated in the hereto effective EEEA.

**The Energy Act also envisages sizable relief for the investors in the sector.** The licensing regimes for the construction, expansion and putting out of operation of energy projects existing in the EEEA have been eliminated. Thereby a serious administrative barrier to the companies in the sector has been removed. The objective of the amendments concerning the licensing regimes and the organization of competitions is also to facilitate investments and to reduce the state intervention in the sector. Tenders will only be organized when a serious need to build new strategic electricity production capacities has been established, i.e. the available capacities cannot guarantee the security of electricity supply. According to the new legislation, the decision to increase the available production capacity will be taken with priority on the market principle. The companies operating on the energy market will expand their production on the basis of their own analyses of the market condition and their future development strategies. The licenses will be granted after the energy project is completed. Thereby the need to wait for the government authorities to decide that construction of new capacities is imperative, as well as the need to participate in tender procedures has been avoided. That in turn will also help to reduce the costs of the individual electricity production companies per unit of additionally built capacity, which is a precondition for lower prime cost of the electricity produced and lower sale prices and higher profit, accordingly. The facilitated licensing regimes for construction of new capacities largely correspond to the practice in the EU Member States.

The legal framework set in the EA lays the foundations of an entirely new market structure of the electricity sector. The latter will be basically divided in two segments – a market where transactions will only be realized at regulated prices, and a market where transactions will be entirely realized at freely negotiated prices.

**Two new categories of actors are introduced within the regulated market – the public contractor and the public suppliers.** The role of the public contractor is to ensure the supply of electricity to the public suppliers and the consumers connected to the transmission network. The public suppliers in turn will supply electricity to the end-users. The more important thing in this case is that according to the EA the public contractor will continue to exercise his exclusive right to realize electricity import and export transactions until Bulgaria's accession to the EU.

**The electricity traders are new subjects on the free electricity market.** They will buy and sell electricity by direct negotiations with the electricity production companies with free capacity and with the eligible consumers, as well as within the organized market. The latter will be organized by a person licensed for this activity and the public contractor and

the public suppliers will also be able to trade on it along with the above mentioned basic actors. That will basically help to place the electricity sector on a market footing. The efficiency of the existence of purely market relations will be determined by the pace at which the actors will manage to adapt, as well as by the availability of administrative and technical capacity for regulation of these activities by the State. The latter also brings forward the question of the need of information on these issues in the future.

**The EA applies the same market restructuring scheme in the gas supply sector.** The Act offers a regulation of the gas market where the gas-production companies, the traders and the eligible consumers have the right to sign contracts with one another, independently negotiating the terms and conditions of supplies. Along with that, the draft law requires them to also close deals with the transfer company with a view to ensure a balanced market. All other natural gas supply transactions are realized within the regulated market under terms and conditions approved in advance by SERC. The Act provides for liberalization of the natural gas import, allowing the traders and the eligible consumers to independently close deals with suppliers outside Bulgarian territory. Gas-production companies will be able to independently export natural gas for foreign customers, but only if they build their own gas pipelines to those customers.

The fundamental changes, which the EA sets forth in the energy and gas market field, include: executing regulated access of third parties to the networks and separating the operational from the business activities of the companies serving the energy sector. That in turn should result in more efficient management of these activities and much higher quality of the services provided.

**The new point in the heat supply sector** is the opportunity for the consumers in a condominium building to set up associations. The latter will be registered under the Non-profit-making Legal Entity Act and will have the right to sign heat purchase contracts at preferential consumer prices. This initiative would generate positive effects for the consumers as well as for the heat supply companies. The latter will not have to communicate with the individual consumers, collect the accumulated debts or perform a lot of other tasks, which currently require significant human resources and time. These obligations will be largely transferred to the associations. Consumers will have to devote time and efforts, which will result in many financial and non-financial costs. The requirement that all owners and users of apartments in the condominium building should be members of the association seems hardly achievable. This is so because of the frequent change of the owners and users in many buildings as a result of the intensive real estate market. The combination of these factors could considerably reduce the net effect of the operation of these associations and put barriers to their dissemination.

**Increasing the green energy** as an instrument to guarantee the security of supplies and the quality of life is among the leading goals of the EU in the energy sector. With Directive 2001/77/EC<sup>20</sup> the European Union requires the member states to take active measures to promote the use of renewable energy sources and sets two indicative objectives for the share of these sources in the total electricity production of each state: 12 per cent in 2010 and 22.1 per cent in 2020. The measures to attain these objectives, laid down in the EA, concern the mandatory buy out of the energy produced, preferential prices and priority connection of the producers of electricity from RES and according to combined methods to the transmission and distribution networks. These measures will remain in force until the system of trade in green certificates is introduced. Within the system, the Minister of Energy will determine a minimum mandatory share of electricity to be produced from RES or according to combined methods. The companies, which cannot achieve the requirements with their own production, will buy green certificates.

The positive effect, which may be expected from the privileges laid down in the Act, is lower dependability of Bulgaria on the import of energy resources through higher share of the electricity produced from RES. These measures will also contribute to higher security of the investments in RES energy production. In principle such investments have a long period of redemption owing to the large initial production capacity construction costs and the rather low production capacity. The higher security may also result in better terms of raising funds for the construction of such electricity power plants. The higher share of the electricity and the heat produced from RES will help to improve the environmental situation in Bulgaria through lower emissions of greenhouse gases to the air.

Buying **green certificates** will force the producers, who are unable to secure their mandatory quantities of energy produced from RES, to incur additional costs. That will increase the prime cost of their production and will lower their competitiveness.

**The Memorandum of Understanding on the Regional Energy Market in South East Europe and its integration into the European Community Internal Energy Market**, signed in Athens, was an important event for the Bulgarian energy sector in the last quarter of 2003. The following countries signed the Memorandum: Bulgaria, Albania, Bosnia and Herzegovina, Croatia, Romania, Turkey, Serbia and Montenegro, Macedonia and the United Nations Mission in Kosovo (UNMIK). Greece, Austria and Italy are political actors in the process having all rights and obligations under the Memorandum, whereas Hungary, Moldova and Slovenia signed the document in the capacity of observers.

<sup>20</sup> Directive 2001/77/EC of the European Parliament and of the Council of 27 September 2001 on the promotion of electricity produced from renewable energy sources in the internal electricity market [http://europa.eu.int/eur-lex/prl/en/oj/dat/2001/l\\_283/l\\_283200111027en00330040.pdf](http://europa.eu.int/eur-lex/prl/en/oj/dat/2001/l_283/l_283200111027en00330040.pdf)

The objective of this initiative is to create a regional energy market by gradually approximating the energy policies of the individual states mainly in the electricity and the gas sectors. The states, which signed the Memorandum, will have to establish uniform rules of production, transmission and distribution of electricity and gas and to apply the market organization and functioning mechanisms laid down in the European directives. The deadline for implementation of the rules and the principles laid down in the Memorandum of Understanding is 1 July 2005.

The establishment of a regional energy market, which actually means liberalization of the trade in electricity and gas between the countries that have signed the Memorandum, will create conditions for serious competition. The positive results such as lower prices, higher quality of services, and the other effects of competition will certainly not be delayed. The place each state will manage to take on the regional market will depend on the pace of development of the energy sector in the individual countries – building substitute and new production capacities, developing the transmission networks, reducing technical losses, having the producers and consumers improving the energy efficiency by producers and consumers, etc.

in turn undertook to send an expert mission to establish the implementation of the specific recommendations to Bulgaria in the 2001 and 2002 reports of the Atomic Questions Group and the Working Party on Nuclear Safety at the European Council.

The implemented peer review generated serious debates in the public space. Two basic proposals to extend the operational period of the two units were launched – to reopen the Energy Chapter or to renegotiate the time limits in the final phase of the negotiations. Despite the demonstrated willingness to develop a common position on this issue, harmony of opinions and political consensus were not achieved. At the same time, the external political pressure to close the units becomes increasingly stronger. Under these circumstances the efforts should be focused on maximization of the compensations Bulgaria must receive for the close down of the two units.

An official start of the **privatization of the seven electricity distribution companies (EDC)** was given in the last quarter of 2003. Sixty-seven per cent of the shares in each EDC, distributed in three packages, will be privatized by way of public tender process (Table 17). The candidate buyers will

Table 17. Data about EDC packages

Indicator	Northeast Bulgaria Package		Southeast Bulgaria Package		West Bulgaria Package		
	Gorna Oriahovitza EDC	Varna EDC	Plovdiv EDC	Stara Zagora EDC	Pleven EDC	Sofia District EDC	Sofia City EDC
Area of the region served, km <sup>2</sup>	15 623	14 360	20 000	21 000	19 613	19 093	1 311
Network length, average voltage and low voltage, km	22 926	18 298	32 706	23 245	23 431	20 775	10 348
Total number of customers	539 252	591 747	856 244	630 193	600 125	593 327	661 839
Electricity supplied, GWh	2 300	2 471	3 572	2 728	2 175	1 904	3 414

Source: MEER, [www.doe.bg](http://www.doe.bg)

**The basic conclusion of the EC about the progress achieved in the energy sector** against the last regular report is that Bulgaria continues its progress in the reform and preparation of the sector in compliance with European requirements, including those concerning the country's future participation in the internal energy market. According to the report, Bulgaria must focus its future efforts on improving the administrative capacity in the sector, on the full and timely harmonization and implementation of the European legislation, on energy efficiency and the use of RES, on creating the required reserves of oil and oil products, as well as on the preparation to close and take out of operation the units of Kozloduy NPP determined in the negotiation processes. Bulgaria must continue to implement its sector restructuring plans, taking account of the social effect of the latter.

In accordance with the agreements reached in the negotiations with the EU, **a technical inspection of the nuclear safety at Kozloduy NPP was carried out in November**. Closing the Energy Chapter, the Bulgarian side undertook to take out of operation unit 3 and unit 4 of Kozloduy NPP in 2006. The EU

be able to bid for the three packages simultaneously, but will acquire one package only. The competition procedures started with candidate buyers purchasing the tender documents and selection of those of them who cover the minimum eligibility criteria for participation in the tenders. The time limits for the individual phases of the competition procedures were extended twice and finally 16 February 2004 was fixed as a deadline for submission of indicative offers by the companies admitted to the first phase. Five big foreign companies submitted offers – EVN, PPC, Enel, CEZ and E.ON. Having examined the offers of each participant, the competition commission must prepare a report on the basis of which PA will select the finalists, who will participate in the final phase of the tenders. In that phase every admitted candidate will have right of access to the available information about EDCs' activity, which will allow the candidates to make full analysis of the individual projects and develop accordingly their final offers.

The privatization of the EDCs is in line with the basic guidelines for development of the sector laid down in the EA and Bulgaria's Energy Strategy. It is expected to attract strategic companies

to the Bulgarian energy market. The objective is to secure in this way the necessary volumes of investments in the electricity distribution network, thereby reducing the losses from the transmission of electricity to the end-user (thefts included), improving the efficiency and the quality of the service offered, and improving the general well-being of the end-users in the long run.

In the last quarter of 2003 NEK EAD on one part and Verbundplan GmbH and Alpine Mayreder Bau GmbH (Austria) as project contractors on the other part signed **the contract for design and construction of the Tzankov Kamuk Hydrosystem**<sup>21</sup>. The project envisages construction of a dam lake and a HPP with installed capacity of 80 MW. The annual electricity production of Tzankov Kamuk HPP is projected at 185 million kWh. The plan is to use this electricity to cover peak and sub-peak loads, as well as for immediate reserve in the event of problems with some basic capacity. The project value is about EUR 200 million to be secured by loans from Bulgarian and foreign banks. The hydrosystem will be constructed within the Memorandum of Understanding<sup>22</sup> on the bilateral cooperation of Bulgaria and Austria for implementation of joint projects in fulfillment of the Kyoto Protocol. That enables to have the loans provided without state guarantees and at lower prices.

The project will help to generate employment in the region during the preparation and construction phases, as well as after the complex is put into operation. Possible orders towards Bulgarian companies, which will be subcontractors of construction materials, transport services and of the other infrastructure building activities, will have a positive effect on Bulgaria's economy. The electricity produced by the hydroelectric power plant will help to reduce the emissions of greenhouse gases to the air. The "Reduced Emission Units" will be sold to Austria at prices per ton, which actually means higher revenues for the State.

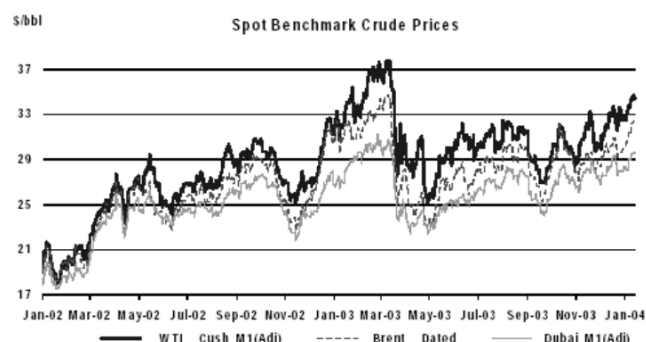
The positive effect of the hydrosystem's operation will also be dependable on the future meteorological conditions. The latter will determine the river's high water and the load of the hydroelectric power plant's production capacity.

## Energy Prices

In the last quarter of 2003 **international market crude oil quotations** remained unstable, with the Brent oil price per barrel fluctuating within the range of USD 27 – 31 (Figure 21). Having continued firm at the level of USD 27 per barrel in October, in November the prices exceeded the level of USD 28. The year ended at a level of USD 29 per barrel, registering an increase of 7 per cent for the whole period under review. The oil price

increase was accompanied by depreciation of the US Dollar, which registered a drop of 6 per cent within the last quarter, reaching the rate of BGN 1.57 = 1 USD at the end of 2003. The decisive factors for crude oil prices included again the news from the Middle East, the North Sea oil production levels, and the USA oil and oil products production and reserves.

Figure 21. Spot Crude Oil Price Dynamics for WTI, Brent and Dubai Grades



Source: Monthly Crude Oil Price Report, International Energy Agency, January 2004, <http://omrpublic.iea.org/currentissues/full.pdf>

The situation on the international oil markets also has effect on the Bulgarian economy, because Bulgaria satisfies almost all of its needs from import under trade conditions following international market dynamics. That resulted in higher end prices of fuels on the Bulgarian market.

An event, which will have effect on fuel prices in the new 2004 is the increase of the excise duty rates since the beginning of 2004 (Table 18), laid down in the amendments to the Excise Duty Act. The harmonization of the national with the European legislation was pointed out as the basic reason for the increase.

Table 18. Fuel excise duty rates in the EU and in Bulgaria

Fuel type	Excise duty, EUR per 1000 liters		Difference
	EU since 1 January 2004 (minimum rate)	Bulgaria since 1 January 2004	
Leaded gasoline	421	253	-168
Unleaded gasoline	359	253	-106
Diesel fuel	302	202	-100
Propane-butane	125	174	+ 49
Kerosene	302	202	-100

Source: European Commission (<http://europa.eu.int/comm/>) and Act on the amendments to the Excise Duty Act

It should be noted that Bulgaria does not differentiate yet the excise duty rates for the fuels used for different purposes. In the EU the excise duty on one and the same type of fuel varies depending on whether the fuel is used for cars, for industrial purposes, or for heating. Fuels for cars have the highest excise duty. Table 18 reveals that Bulgaria is still far from the minimum

<sup>21</sup> For more details see the section on Environmental Policy.

<sup>22</sup> Signed in September 2002 in Johannesburg.

<sup>23</sup> Mazut with 1 per cent sulfur content, mazut with 3.5 per cent sulfur content and gas oil with 0.2 per cent sulfur content.



excise duty rates for fuels (used for cars), except for the propane-butane rate, which is higher than the EU minimum.

The lower alternative fuel<sup>23</sup> quotations at the international markets in the fourth quarter, which have effect on the import **price of natural gas** in Bulgaria, and the depreciation of the US Dollar resulted in an average decrease of about 9 per cent of natural gas prices for the consumers connected to the transfer and distribution network of Bulgargas since the beginning of 2004. The decrease will mostly affect the basic consumers including the fertilizer, glass, oil, cement and ceramic industries. Natural gas price changes will also help to lower the costs of the district heating companies as they are in the season of peak load of their capacities and are buying and using maximum quantities of natural gas. The lower prices will help to lower the variable costs of the state company's big customers. That will result in upturn of their market positions and profit opportunities depending on the price elasticity of their production.

In contravention with the lower gas prices, SERC approved higher prices of the heat supplied by Toplofikatzia Sofia AD (Sofia Heating Company AD) since 1 January 2004. The one-component price of the thermal energy is increased from BGN 58.87 per megawatt-hour to BGN 61.85 per megawatt-hour. Two-component price is changed from BGN 35.27 per megawatt-hour to BGN 38.27 per magawatt-hour and the output price for power per cubic meter and per kilowatt is also increased by an average of 8 per cent.

In the past quarter the transport sector did not witness any developments towards substantial progress in the sector's restructuring or evolution. The focus was placed on changing the sector's legislative framework and on the sale of Varna Dockyard. The State demonstrated willingness to allocate sizable resources to improve the transport infrastructure quality.

**The Amendments to the Road Act, voted on first reading,** were a key event in the last quarter of 2003. The basic changes laid down in the voted draft law concerned introduction of a vignette system for using the national road network, and creating conditions to concession republican roads, parts thereof, or individual facilities. The major objective of the changes is to attract private investments for construction.

According to the texts passed by the National Assembly, transport vehicles will pay a **vignette charge**, which grants the right to use the road network for certain period of time. Vignette charges will be introduced step by step for Bulgarian and foreign vehicles. First their amount will be different, and the equalization should be completed by the date of Bulgaria's accession to the EU.

The draft law envisages that the charges collected under the new system shall only be spent for operation, maintenance, repair and reconstruction of the republican road network. The possibility to spend them for construction of new road infrastructure is excluded. **A Republican Road Infrastructure Fund** to accumulate the revenues from the vignette charges **will be set up** for better system functioning. The Fund will be managed by a Managing Board having the Minister of Regional Development and Public Works as president and the deputy-ministers of finance, internal affairs, transport and communications, as well as the Executive Director of the Road Executive Agency, as members.

The positive aspect of the transition from a road tax to a vignette system is the option to choose the time duration limit for which the charge is paid. There are three options – weekly, monthly and annual vignette charges. Thereby transport companies, as well as households, will have greater flexibility in cost management as the need to pay an annual charge irrespective of whether you use the road infrastructure or not will be eliminated. On the other hand, that could increase the transaction costs of companies, which buy vignette stickers, owing to the need of more frequent communication with the administrative body when using vignettes other than annual ones. Taking the financial operations for road repair and rehabilitation out of the budget is a positive fact. It will contribute to the more efficient and result-oriented utilization of funds, given that they will not pass through the state budget whereby the possibility to allocate for another type of government expenditure the money paid for road quality improvement will be eliminated.

Given that the revenues in the Republican Road Infrastructure Fund will not be used for construction of new roads and facilities, while there is a need of the latter, the draft law **also regulates the introduction of charges for passed road section or for the use of a road facility**. The direct collection of such charges is expected to make investments in the construction of some road infrastructures, such as highways, tunnels, bridges, etc., more attractive for the private capital. The Council of Ministers will determine on a proposal by the Minister of Regional Development and Public Works the roads to be given on **concession**. The draft law lays down as an incentive for investors the option that the Council of Ministers shall release the concessionaire from the obligation to pay concession charges, depending on the project efficiency, the necessary construction costs, the traffic, and the amount of the pass charges.

The attempts to attract private capital through public-private partnership in the construction of Bulgaria's road infrastructure are a good undertaking, which should mean that the road network financing and management are based on market principles. That, however, implies that the pass charges for concession roads should be determined by the concessionaire, whereas the current plan is to have them determined on the basis of a tariff developed by the Council of Ministers.

The draft law was finally passed in early 2004.

**A draft law constituting amendment to the Civil Aviation Act** was put to discussion in the National Assembly in the past quarter. The key points in the draft concern the set up of conditions for competition in the ground services and of opportunities to concession the management and operation of civil airports.

The draft law envisages that ground services shall be carried out by traders registered under the Commercial Act and licensed as ground service operators. The plan is to issue **ground service licenses** to all applicants, who satisfy certain requirements defined in advance, with everyone who has received such license having right of access to the ground service market. Licenses shall be issued by the Civil Aviation Administration General Directorate. The latter will also exercise the ex-post state control of the implementation of the obligations under the licenses issued.

The rules laid down in the draft law help to harmonize Bulgarian regulations with European requirements. Creating an environment for competition is also a positive step forward in the air transport development. It would have a positive effect on the quality of service in the Bulgarian airports, which is a precondition for the dynamic development of national tourism.

The draft law specifies the terms and procedure of **granting concessions on civil airports**. Concessions will be granted by

way of tenders and competitions on a proposal by the Minister of Transport and Communications put forward in the Council of Ministers. An option for the concessionaire to collect in full or in part the charges for the activity he carries out is also provided.

Granting concessions on airports is expected to attract investors who will provide the necessary funds for reconstruction and development. Making concessions on airports is also associated with the opportunity to improve management and operation by way of attracting private companies having experience in the sector. Granting concessions on public airports will also change the revenues in the state budget from this activity. The amount of these revenues will be dependable on the concession charges, which the concessionaire will have to pay, on the share distribution of the service taxes between the State and the concessionaire, and indirectly by the corporate tax the concessionaire will pay to the budget.

The idea to considerably increase the funds to be spent by the State in 2004 for improvement of the transport infrastructure was launched in the last quarter of 2003. The plan is to allocate BGN 500 million from the fiscal reserve account<sup>24</sup> to increase the capital stock of the Highways State Company in the form of "compensatory financing". The individual infrastructure projects and the financing amount for each project remained unspecified. This may have a negative effect on the possible future spending of the funds from the state budget. The question of whether these plans will be implemented in practice will probably be solved in the second half of 2004.

EC's recommendations in the latest Report on the progress of Bulgaria are focused on enhancing the administrative capacity in the transport sector. It is necessary for the further adoption and application of the European legal rules and for the implementation of the serious investment plans in the sector.

In the quarter under review the water transport sub-sector witnessed the **sale of Varna Dockyard**. Bids were invited for 75 per cent of the company's assets. Ares Commodities UK Limited – London, Bulyard Consortium, Tzakos Bulgaria and AKB Fores filed applications for participation in the procedure. Bulyard submitted the highest offer and became an owner of the dockyard against USD 16.666 million. The buyer undertook to invest in the company USD 17.7 million within the next three years.

<sup>24</sup> For more information see the Fourth review of the "stand-by" agreement with the IMF, <http://www.imf.org/external/pubs/ft/scr/2004/cr0435.pdf>

The last quarter of 2003 did not bring any significant changes in the high technologies and communications sector. The good news was the first registration and public sale of shares of a technological company at the stock exchange. The Bulgarian e-Government topic was again in the focus of attention, but this time without any significant development or actions on the part of the parties involved.

The eighth **exhibition of information and communication technologies BAIT EXPO**, which has become a tradition, was organized at the end of October. This time the exhibition involved 110 Bulgarian and foreign companies from all ICT sub-sectors – hardware, software, communications, networks, Internet, system integration, and services. The organizers report the event as a big success in terms of the number of visitors and the interest it aroused.

An interesting BAIT-launched initiative was the campaign for popularization and public support of the **Home PC Program** developed by the association to encourage the mass entry of PCs in the homes of Bulgarians. For a little more than two months 4374 people joined the program and over half of them voted for it in the site of BAIT. The idea of the campaign is to lobby for recognizing the purchase of computer equipment and software for home purposes as an investment cost to be deducted from the taxable base. BAIT is also preparing a document with program implementation proposals, which will be presented to the Council of Ministers in 2004.

Official statistical data about the **volume of advertisement in the Bulgarian Internet space** are not available, but most observes and advertising agency representatives share the opinion of sizeable growth in the past 2003. According to the estimates of experts in the field, the Internet advertising market accounts for about BGN 1.5 million, registering a double increase compared to 2002. At the same time the on-line advertising accounts for only 2 per cent of the whole advertising market, but the upward trend is expected to continue in 2004 at a higher pace owing to the growing national Internet audience and the facilitated access to the global network.

By Decision No. 718/21 October 2003 the Council of Ministers approved the Memorandum of Understanding between the European Community and the Republic of Bulgaria concerning Bulgaria's participation in the multi-annual Community program promoting the development and use of the European digital content of the global networks and encouraging the language diversity in the information society (**the eContent Program, 2001 – 2004**). The program is market-oriented and supports projects for the production, use and dissemination of European digital content and for encouraging the multilingual and multicultural aspect of the global information network. The program budget is EUR 100 million. According to the agreement Bulgaria must pay a participation fee of EUR 46 000 each for 2003 and 2004.

The eContent program targets all organizations operating in the digital content area – developers and owners of content in the private and the public sector, designers of the forms in which the digital content is “packed”, language specialists and experts engaged in content adaptation (customization), publishers and distributors, companies providing services on the Internet, copyright organizations, capital market actors and other experts.

The eContent program has three basic action lines:

- Improving the access to and the use of information from the public sector;
- Promoting the development of content in a multilingual and multicultural environment;
- Higher digital content market dynamics.

**The Strategy on improving the competitiveness of Bulgaria's ICT sector on the international markets**, which was under preparation since early 2003, was officially presented at the end of the year. The idea of the document is to reveal the importance of the sector for Bulgaria's economic development and to outline some basic measures targeting improved competitiveness of the companies in the sector. According to the main document drawers (BIBA, BAIT, and BASSCOM) Bulgaria has every chance to become a technological leader of the Balkan region and it should be quick in making use of this advantage. The strategy was later approved by the members of the Council for Economic Growth, who confirmed their acceptance of the fundamental ideas in the document and declared again their support of the Government's intentions for priority development of the ICT sector.

On 25 November 2003, exactly a year after the eGovernment Strategy was passed, **a workshop on the Bulgarian eGovernment and the ICT Sector Development Strategy** was organized in the National Assembly. The idea of the workshop was to acquaint the deputies with the basic characteristics and notions of the eGovernment, with the strategic framework for its development, and with its benefits. This training was organized with some delay, but it is expected to be of use to the members of parliament by helping them to realize the advantages of the use of ICT and having a corresponding positive effect on their work.

At the end of 2003 the Institute of Public Administration and European Integration and the Coordinating Center for Information, Communication and Management Technologies at CoM organized for the first time **a national competition for achievements in the eGovernment field (Online Services 2003)**. The objective of the competition was to support the dissemination of the good implementation practices of various eGovernment aspects in the Bulgarian public administration. Seventeen administrations took part in the competition, 6 of which competed in the Interactive Services category, 6 – in the Information Services category, and the other 5 – in both



categories. A large number of the services presented in the competition are part of the 20 indicative services under the eGovernment strategy. Most of them are still at an early stage of development and are yet to be improved and expanded. Nevertheless, the positive fact is that talks about the electronic administrative services are more frequent in Bulgaria and a field for exchange of experience and discussion of best practices is provided.

At the same time **the Sofia City Internet Site was ranked 36 in the first evaluation survey of the digital government in the biggest towns of 98 UNO Member States.** The towns were selected from the database of the International Telecommunication Union on the basis of the percentage of the citizens using Internet and the number of the population. The Internet sites were evaluated on the basis of 92 indicators united in five key areas: information security and protection, level of use, content, provided services, civil participation. Cities like Berlin (38), Brussels (45), London (55), and Moscow (66) are ranked below the capital of Bulgaria. It is a fact that the Internet users in Sofia account for 40 per cent of the capital's population, which certainly contributes to the good ranking of the city.

In the beginning of November Eurostat published **information about the employment in the production of high and medium high technologies and in the so-called knowledge-intensive services (KIS – services, the quality of which is dependable on knowledge).** The data published are for 2002 and cover the EU Member States and the accession countries.

In 2002 a little over 12 million people in the EU were engaged in the production of high and medium high technologies. Germany accounts for the highest share of employment in this type of production (11.4 per cent), followed by Italy and Finland accounting for 7.4 per cent each (which is the average value for all EU Member States). Slovenia accounts for the highest share among the accession countries with 9.2 per cent, followed by the Czech Republic, Hungary and Slovenia.

About 54 million out of the 111 million people in the EU engaged in the services field work in the KIS sector. These services account for 47 per cent of total employment in Sweden, 44 per cent in Denmark, and 40.8 per cent in Great Britain. Estonia performs best among the accession countries (30.9 per cent of total employment in the country) followed by Hungary and Cyprus (26.4 and 26.2 per cent, accordingly).

Bulgaria performs rather well against the countries covered by the survey. Out of the total employment of 2.8 million people, 5.3 per cent are in the high and medium high technology field, which ranks Bulgaria fifth among the countries outside the EU. The people employed in KIS are a little over 1/5 (22.2 per cent of total employment), but according to this indicator Bulgaria occupies the unenviable one from the bottom place before

Romania. Table 19 contains data about the future EU member States.

Table 19. Distribution of employment in selected sectors, %, 2002

Country	Total employment (thousand people)	High and medium high technological production	Other production	Other (production and services excluded)	Other services	KIS
Czech Republic	4 763	8.9	19.1	17.0	31.2	23.9
Estonia	581	3.4	18.6	15.4	31.8	30.9
Cyprus	315	1.1	11.1	16.2	45.4	26.2
Latvia	988	1.9	14.5	24.5	34.4	24.7
Lithuania	1 421	2.6	15.2	28.2	29.3	24.7
Hungary	3 846	8.5	16.4	15.3	33.3	26.4
Slovenia	922	9.2	21.9	17.0	29.1	22.8
Slovakia	2 111	8.2	18.8	17.7	31.2	24.0
Bulgaria	2 800	5.3	18.5	19.5	34.5	22.2
Romania	9 768	5.5	16.0	45.8	19.9	12.8

Source: Eurostat

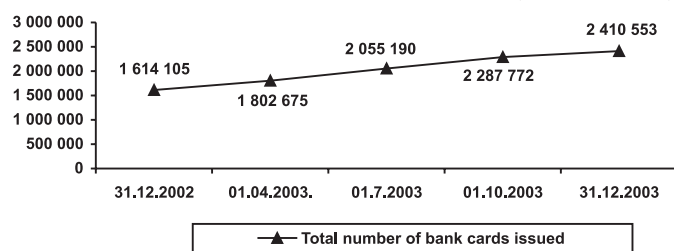
The good performance of the country in the high technology and KIS field is a serious precondition for ensuring fast economic growth. In the last quarter of 2003 there was much talking about prioritization of the ICT sector (which is part of the technology sector and of the knowledge-based economy) and making declared intentions a reality would certainly help to improve Bulgaria's economic indicators.

**The first registration of an ICT company on the stock exchange** became a fact at the end of 2003. On 26 November FSC entered Bulgarian Information Technologies AD (Bitex.com) in the register of public companies. On 9 December Bulgarian Stock Exchange – Sofia AD accepted for trading an issue of the company (2.9 million shares each with a face value of BGN 1). The company is owned by the Greek Promota Hellas SA, registered on the Athens Stock Exchange, and by three physical persons. Promota Hellas was established in 1996; in 2000 it was acquired by the American company Worldfast Communications Inc., and three years later Promota Hellas acquired a majority interest in Bitex.com and contributed to the further investments in and growth of Bitex.com. The company's main scope of business is alternative telephony, Internet services and software development.

The emergence of a high-tech company on the stock exchange is a good sign for the ICT sector development and might be implying that other companies will soon follow this example. A factor for that will be the new opportunities opening for the telecommunication operators licensed in 2003, who will need sizable financial resources to carry out the planned expansion of the business.

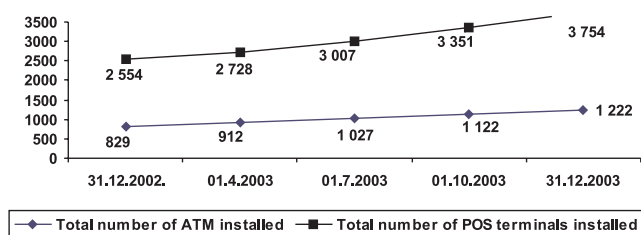
Although the growth rates are not as remarkable as in previous periods, in the last quarter of 2003 the data by the national card operator Borica AD reveal again a positive trend in this segment of the ICT sector (Figure 22 and Figure 23). The total number of ATM and POS terminals installed and of bank cards issued in the fourth quarter registered again an average growth of about 9 per cent (8.91 per cent for ATMs, 12.02 per cent for POS terminals, and 5.36 for cards, accordingly).

Figure 22. Total number of bank cards issued (2002 – 2003)



Source: Borica AD (www.borica.bg)

Figure 23. Total number of ATM and POS terminals installed (2002 – 2003)



Source: Borica AD (www.borica.bg)

Data about the transactions via Internet, ATM and POS terminals in 2003 reveal much higher growth. Total transactions via Internet registered more than double growth compared to 2002, and the information about ATM reveals a growth of almost 3.5 times compared to 2002. The number of transactions via telephone registered the lowest growth – only 13.85 per cent.

The statistics of the total amount from transactions in 2003 also reveal improvement, though not at such high pace. For the whole 2003 payments via Internet amount to over BGN 3.3 million, registering a double growth compared to 2002. The growth for ATM is higher again – BGN 3.8 million or almost 4 times (Table 20).

Table 20. Transactions via Internet, ATM and telephone

Total transactions performed	2002	2003
Total transactions via Internet (ePay.bg system)	36 441	90 501
Total transactions, payment of services via ATM	35 071	120 785
Total transactions, payment of services via telephone	12 018	13 683
Total amount from transactions, in BGN	2002	2003
Total amount from payments via Internet	1 608 733.11	3 329 803.28
Total amount from payment of services via ATM	1 116 858.19	3 779 513.35
Total amount from payment of services via telephone	423 876.96	512 662.24

The steady growth registered by these indicators reveals increasingly higher confidence in the electronic modes of payment, which is a positive sign for ICT development. This fact is also significant for the future development of the electronic business and the eGovernment, which should become an integral part of the daily life of citizens and the business.

### Number of Tourists and Revenues from Tourism

According to data by the Ministry of Economy, the number of foreign tourists who visited Bulgaria in 2003 registered an increase of 18 per cent compared to 2002. Revenues from international tourism amounted to USD 1.622 billion, registering an increase of 21.6 per cent.

The above data reveal that Bulgaria ranks among the first in Europe in terms of tourism growth dynamics. According to the World Tourism Organization, Bulgaria is one of the most rapidly developing tourist destinations. The results achieved in this field are particularly significant against the unfavorable development of world tourism, which registered in 2003 the most sizable drop for the last few years.

According to information by MoE, **in 2003 the number of foreign tourists reached 4.04 million people.** Greece, Germany, Great Britain, Russia, and the Scandinavian countries account for the highest number of tourists. Tourists from Greece reached 547 thousand people, and those from Germany – 534 thousand people. Most significant is the growth of the number of tourists from Greece – 39.9 per cent, Great Britain – 43 per cent, Germany – 11.2 per cent. Tourists from Holland also registered an increase by 31 per cent, as well as those from Sweden and Finland – by 28 per cent each.

The fact that **Bulgaria gradually restores its positions on the Eastern European countries' market** is positive. Tourists from Russia registered an increase of 22 per cent; the fact that the number of tourists from the Czech Republic registered an increase of 62 per cent, and from Slovakia – of 50 per cent, is also satisfying. Tourists from Hungary registered the most significant growth in this category – by 104 per cent.

The positive trends of tourism development continued **in the fourth quarter of 2003 when revenues from tourism reached USD 237 million**, registering an increase of 29 per cent compared to the same period of 2002 when they amounted to USD 183.4 million.

In the fourth quarter of 2003 **Bulgarians' spending on tourist services abroad** also registered an increase of almost 30 per cent compared to the fourth quarter of 2002 and reached USD 184.3 million. **Net revenues from tourism amount to USD 52.7 million.**

In the past year, including the fourth quarter, **the good results were preconditioned by** several circumstances. These include in the first place the investments made by the private sector in the special infrastructure and the parallel improvement of the conditions offered to the foreign tourists. Second, Bulgaria was not seriously affected by two major factors, which had effect on global tourism development – the war in Iraq and the cases of

heavy respiratory syndrome which resulted in overall drop of travels all over the world.

Bulgaria's proximity to Greece where the 2004 Summer Olympic Games will be organized can be added as a prospect to the favorable preconditions outlined above. This circumstance is associated with the sportsmen training opportunities, which Bulgaria provides, with popularization of the good aspects of Bulgaria's tourist product and looking for ways for further visits after the end of the games in Athens.

### Investment Activity and Special Infrastructure Development

**The active winter season** started in the fourth quarter of 2003. There are a number of preconditions for its successful development, the investments made in all winter resorts in the first place. The new cable car running from **Bansko** to the Bunderishka poliana locality in Pirin was officially opened at the end of 2003. Its total length is 6 315 m, and the capacity – 2 400 people per hour. The successful implementation of this project made Bansko the most modern Bulgarian winter resort. This is also the biggest investment in a winter resort, amounting to EUR 30 million. More than 80 per cent of the ski tracks here have artificial snow equipment, which allows for a longer winter season – from November till March. The complex provides opportunities for skiing and snowboarding. Almost 90 per cent of the tracks correspond to the requirements of the International Ski Federation. It is these circumstances that determine the expectations of a good winter season in the resort. Full packages are sold for the whole period; hotel beds are booked, tourists from Germany, Great Britain, Russia, Greece, Macedonia, etc. are expected.

At the start of the winter season investments in **Pamporovo** amounted to about BGN 3 million. The basic portion was invested in renovation and rehabilitation of the special infrastructure. An important point in the new winter season is the return of a leading world tour operator – TUI. A growth of the number of German tourists in Pamporovo is expected. It should be noted that this Bulgarian resort attracts tourists with higher purchasing power from Germany and other countries. Notable is the attempt of the hoteliers and the tourist companies to prolong the active tourist season through the promotion of congress and rehabilitation tourism. The positive practice of hoteliers' uniting in the Pamporovo XXI Century Association contributes to the successful tourism development.

Good preconditions for a successful tourist season exist in **Borovetz**, too, where sizable funds were also invested in the rehabilitation of the tourist resources; snow machines are used, which also allows to prolong the tourist season. A positive trend is observed in this resort as well – Russian tourists are coming back. But Great Britain, followed by Germany, Belgium and Denmark, still account for the highest number of tourists.

## Changes in the Regulations and the Institutional Regulation

**Amendments to the Tourism Act were passed on first reading** in the fourth quarter of 2003. Some of the most important proposals include:

**Set up of a Tourism Agency at the Ministry of Economy.** The existing Agency for National Tourist Advertising and Information will be a member-part department within the Tourism Agency. The plan is to set up two commissions of experts at the Tourism Agency – on the registration of tour operators and tourist agents and on the categorization of sites. Representatives of the Ministry of Economy and the new agency will be involved in these commissions, as well as representatives of the trade organizations, but only where the latter are nationally represented.

Some of the engaged in the sector object to such a decision to set up an agency. They believe that the role of the tourist industry is thereby underestimated. In their opinion the significance of tourism as an important national priority is undervalued and a more convincing option is to create a special Ministry of Tourism or a Tourist Board.

**Another amendment provides for regulation of a nationally represented tourist association** – according to the amendments this will be a legal person uniting not less than 34 per cent of the companies registered to carry out tourist activity in the corresponding field.

This proposal was also criticized by the tourist industry representatives, because at this stage no organization pretending to be nationally representing – BATA, BHRA, BAAT, satisfies this requirement. There were also objections towards the criteria proposed. Yet the set up of such national association would be a positive step, because it will unite at a higher level the people employed by the sector and will be able to protect more effectively their interests.

Changes towards facilitation of the treatment of tour operators and tourist agents by transforming it from licensing into registration one are envisaged. Changes in the categorization of tourist sites are also contemplated.

Discussions on the amendments to the Tourism Act continued in the beginning of 2004.

## Marketing and Advertising. Events and Forums

**The first regional Conference on Biodiversity and Ecotourism in Southeast Europe** was organized in Sofia in November. Representatives of non-government organizations, experts and companies in the tourism sector from Bulgaria, Macedonia, Albania, Bosnia and Herzegovina, Croatia,

Serbia and Montenegro, and Romania took part in the forum. The event is important for making the Balkan region a successful destination for ecotourism. The good private sector – government institutions partnership in the preservation of the biodiversity and the protected territories at local and regional level is a good precondition for that. The forum organized is expected to result in presentation and implementation of joint projects for development of regional tourist products based on the natural and the cultural and historical resources of the countries in the region.

**A national tourism and leisure time fair** was organized in Varna in November again. The focal points of this exhibition included the novelties in the tourist product, the opportunities and advantages of building a national booking system, the presentation of tourist destinations in different Bulgarian regions and some new tourist destinations in South Africa. Questions concerning the barriers to Bulgarian tourist industry development were placed at the forum – the poor quality of the transport and technical infrastructure in the first place, followed by the poor quality of the personnel working in the sector, the absence of professional management, problems with the hygiene and the bad treatment of tourists. Legal regulations are harmonized with European ones, but problems in the implementation of laws do exist.

It was announced at the forum that a uniform national tourist information database will be built, which is expected to considerably improve the popularization of Bulgaria. Unfortunately, the start of such database has been repeatedly announced, but has not become a fact yet.

Bulgarian companies also took part in the **tourist exhibition organized in London** in November. **The start of an official representative Bulgarian tourism site ([www.bulgariatravel.org](http://www.bulgariatravel.org))**, which was demonstrated at the forum, was an important point in the presentation of the country and the popularization of its opportunities as a tourist destination. The site provides comprehensive information about the potential of the Bulgarian tourist industry, about sights, transport conditions, advertising brochures, etc.



## Condition of the Sector

Along with the compensated damages from the poor crop in the grain sector and the provision of the necessary funds for the autumn sowing in a short-term perspective, the fundamental problem for agriculture in a long-term perspective remains the land reform, which is delayed and impedes the development of the whole sector. The downward trend in the share of agriculture in the gross value added and the gross domestic product is preserved and, according to preliminary estimates, in the fourth quarter of 2003 this share amounts to 8 – 9 per cent of GVA and less than 8 per cent of GDP. The positive balance of the foreign trade in agricultural products is preserved against the growing total deficit of the trade balance.

The poor grain crop and the problems it generated encouraged farmers to get more actively involved in the **autumn sowing**. The favorable sowing conditions and the fact that sowing was completed on time give grounds to project that sown areas will register an increase compared to 2002 (9 million decares). The measures taken by the State Agriculture Fund envisage subsidies for pre-sowing fertilizing and for purchase of seeds and fertilizers. Additional BGN 2 million were allocated for fertilization of the areas sown with wheat alone. As a result of these measures, more than half of the areas will be supported for fertilization.

Unlike the grain crop, **the grape crop** proved better than expected and allowed to secure for processing about 260 thousand tons of grapes (an increase of almost 50 thousand tons compared to 2002 and 30 thousand tons above the initial projections). Besides, the crop is of exceptionally good quality, which will make possible the production of quality wines.

**The census of operating farms** was completed and the data will be entered in the integrated information system by the beginning of April 2004. The analysis of the information about some 860 thousand farms covered by the census is expected to provide opportunities to protect to the maximum Bulgaria's position in the negotiations with the EU on the financial framework and the quotas.

The stagnation on the **land market**, conditioned by a supply, which is three times higher than the demand, and by the great discrepancy between supply and demand prices, persists. There are still transactions for land, which is not used to the purpose, but for construction of industrial and trade facilities. Yet such transactions become less important. A trend of expanding agro-companies' buying land exclusively for farm purposes is observed. Owing to the low price of land and owners' unwillingness to sell in an unfavorable market, lease becomes increasingly important. The absence of a real land market to influence the agrarian sector development was also reflected in the European Commission's Regular Report on the Progress of Bulgaria: "Progress has been made in the land

reform and in the establishment of a farm land register and the corresponding geographic information system, but further efforts are needed in terms of land consolidation with a view to develop an effective land market."<sup>25</sup>

**A pilot project for consolidation of farm land in selected regions** was started. Land consolidation is one of the ways to develop the land market, as it provides opportunities to introduce modern technologies in land cultivation and to develop modern and effective farming. The Project for Consultant Services for Implementation of a Farm Land Consolidation Pilot Project supported by the World Bank and financed by the Dutch Government was started in early October in three villages in different municipalities. The consolidation of fragmented farm land plots will cover private farm estates as well as land from the State Land Fund, the Municipal Land Fund, and land owned by legal persons. The first project plan of the consolidated farm estates in the land of the village of Golesh, Silistra region, which was developed under another project – the Bulgarian-Dutch Consolidation by Agreement in Bulgaria Project launched in September 2002 – was presented in December. These two projects are a serious sign that MAF and the donors will focus their efforts on solving this problem, which is fundamental to the successful restructuring of Bulgarian agriculture.

Another project was launched in October in the forestry sub-sector. The task of the **Bulgaria – Forestry Sector Development Project** is to develop a policy, which will provide opportunities to protect to the maximum the public interests in forest management in a market economy environment. The objective is by way of sustainable management of forest resources to improve their contribution to the national economy and to make the necessary changes to adapt the forestry sector to the requirements of Bulgaria's accession to the EU. The project will be financed with the assistance of the World Bank and its implementation is planned for 2004 – 2010. Amendments to the Forestry Act were adopted to that effect.

## Environment for Development

Assessments of **the effect of government's intervention on the grain market** in the fourth quarter of 2003 are far from synonymous. The intervention quantities (200 thousand tons) released from the Government Reserve and offered on the Sofia Commodity Exchange eased the market and stabilized the price at a level corresponding to the international market situation. From this point of view the government intervention could be regarded as successful. At the same time two other commodity exchanges registered serious imbalance and huge price margin, which prevented the conclusion of real deals. On the other hand, these two exchanges became major suppliers in completing the Government Reserve with imported grain from Kazakhstan, the USA and Canada. In November the

<sup>25</sup> 2003 Regular report on the progress of Bulgaria in the process of accession, page 72 <http://www.government.bg/Europe/News/>

Government took decision for duty-free import of flower in the period January – June 2004 with a view to offset the effects of the poor grain crop. This measure generated protests by the millers as preconditions for unfair competition were created and the market relationship was disturbed. The ambiguous intervention policy of the government, which was oriented towards solving problems “piece by piece” and imposing political/social reasons on the business, as well as the absence of long-term measures to overcome critical situations make the market unpredictable and impede normal market relations. This situation outlines the need to quickly establish and make operational an intervention agency similar to the one in place in the EU.

Given the poor crop of all cereals and with a view to provide fodder for Bulgaria's stock-breeding, a decision was taken for duty-free import of barley, oats and rye in the period January – June 2004 and for maize the term was extended to September.

As a result of the purposefully implemented measures for fulfillment of EU's veterinary requirements, **the ban on the export of live stock from Bulgaria to the EU Member States** was lifted in early November. Only the ban on the export of live pigs and products thereof remains because of the anti-hog cholera vaccine used. Further efforts are taken to increase the number of **food-industry enterprises licensed for export to the EU**. The number of licensed dairies reached 16; another 4 have fulfilled the requirements and are waiting to get licensed. So, hopefully, in 2004 the dairy product export quotas for the European market may be fulfilled for the first time. Three new fish and fish product production and processing enterprises were placed on the list of enterprises approved for export to the EU, whereby the number of licensed fish enterprises reached six.

The work under the **SAPARD Program** continues – 121 new projects at a total value of BGN 146.7 million were approved in the quarter under review, with the subsidy amounting to BGN 68.8 million. The vegetable growing sector accounts for the highest number of projects – 32 at a total value of more than BGN 16 million. The highest amount of funds is allocated for projects for processing of agricultural products – BGN 75 million for 17 projects. BGN 21.5 million are allocated for vine production projects, and BGN 4 million – for perennial plants (orchards and vines). Twenty seven projects at a total value of BGN 14 million are approved in the tourism sector. Projects in the wood-processing and the apiculture sectors are also launched. Along with that, the subsidies for 118 completed projects, amounting to a total of over BGN 26.5 million, were paid in the period 1 October – 1 December 2003. A start was given to the municipal administration training for the preparation of projects under the two new measures (07 and 08, for construction of road and sewerage network, for water supply improvement, for strengthening the inter-urban infrastructure) for which BGN 138 million are envisaged till 2006.

The projects under **MAF's Development of Agriculture in Northeast Bulgaria Program** amounting to a total of BGN 522 430 and targeting basically stock-breeding, development of orchards, lavender and vine tracts, which have already been paid, can also be added to this program. **A grant aid of over USD 891 thousand from the Japanese government for the preparation of a Rural Development Project** has been negotiated for infrastructure building, institutional development of rural municipalities, project micro-financing and co-financing under SAPARD, as well as for a pilot irrigation project.

**The local elections of mayors and municipal councilors** at the end of October were the most important event in the fourth quarter of 2003, which has incontrovertible effect on regional development.

Various institutions, including non-government organizations, organized many meetings, municipal and national forums, where local authorities' achievements during their previous mandate were assessed. Overall, evaluations point out that **local self-government becomes firmly established, with the corresponding achievements and problems.**

**The good achievements** in this field are associated with: the changing legislation, which is under harmonization with European laws, the initiated constructive local – central government dialogue, the expertise accumulated in the municipalities, the organization of municipalities in a national association, the established public-private partnership at local level, the set up network of partnership organizations and programs, the intensified civil participation in the decision-making process, the active involvement of the Bulgarian municipalities in the European integration process, and the partnership with international organizations in the study and application of good practices.

Legislative efforts were focused on distinguishing the powers and cooperation of local and central authorities, on clearly defining the rights and responsibilities of local authorities within their terms of reference, on the financial and property independence of municipalities through increased tax powers and higher independence in the draw up and management of municipal budgets. Information and service centers for citizens were set up in many Bulgarian municipalities during the past mandate, business centers and business incubators became operational, other forms of informing and consulting citizens were also introduced. A partnership network of organizations which support local authorities, local economic development and the establishment of effective self-government, was set up.

**Major problems** are still associated with the underestimated need of active local – central government dialogue, which would accelerate the decentralization and self-government processes.

Most newly elected mayors and municipal councilors declared at the start of their term of office in the fourth quarter of 2003 their readiness to preserve, develop further and enhance the achievements of Bulgaria's local government. The **continuity of governance** question was placed at various forums at the end of 2003. New local government representatives stressed their readiness to follow the continuity in terms of the policy for social and economic development of municipalities, the continuity in the administration and the municipal council, as well as the continuity in the established contacts and their further development.

**The role of the non-government organizations** in the person of the Local Self-government Reform Foundation, the Local Self-government Initiative, the National Association of Municipalities in the Republic of Bulgaria, etc. was particularly useful in the period under review. These organizations proposed many documents necessary for the new authorities – European charts regulating various aspects of local self-government, comments of laws, description of management activities targeting greater transparency and openness of procedures, presentation of good practices and innovative decisions in the local self-government field.

It is important to note that **the newly elected local authorities will bring Bulgarian municipalities in the EU upon Bulgaria's accession in 2007.** A major priority in the work of local authorities will be to prepare municipalities well for full EU membership. The basic problems in this area were outlined as early as the beginning of the mandate at meetings and forums – absence of sufficient information and knowledge of EU structures and decision-making mechanisms, the tasks resulting from the coming accession are not defined, absence of adequate financial, human and administrative resources, not very effective cooperation with the government level.

The work for successful integration into Europe emerges as a major priority for local authorities. That is why **the Conference on Bulgarian Municipalities – Competent Actors in Utilizing EU Funds** received serious support. At the conference the participants had the opportunity to get acquainted with the municipal project financing mechanisms of the pre-accession programs PHARE, ISPA and SAPARD. The basic recommendations and proposals concern several areas: a need of long-term specialized training in the development of projects to be financed from European funds, which also means more information campaigns and discussion forums at local level on the problems of preparation and accession to the EU; improved access to information about the application procedure for EU programs; intensified partnerships between the non-government organizations, the central government and the municipal governments; presentation of successful municipal practices for utilization of the European funds.<sup>26</sup>

**The round table on the Local Economic Development and Marketing of Bulgarian Municipalities Project**, organized in December by FDL SG with the support of USAID had a positive effect on the local economic development policy. The project is focused on supporting the business at local level and development of public-private partnerships. Its objective is to set up business support units, to make better use of the economic potential of municipalities, to improve the business environment and to promote a proactive business development policy. The project covers 14 Bulgarian municipalities.

<sup>26</sup> For more details see the monthly information bulletin of FDL SG, issue 11, 2003.

The specific activities implemented within the project and contributing to the achievement of the project objectives are worth noting: developing a common marketing site of the municipalities; training of experts in local economic development and analysis of municipal economic resources; encouraging municipal investment activity; developing and implementing business support programs; drawing up local economic development plans, preparing marketing materials and participating in fairs and exhibitions.

### **The started implementation of the decision to authorize the municipalities to collect alone the local taxes and charges**

is an important specific step towards greater independence of local authorities. According to the amendments to the Local Taxes and Charges Act, municipalities should collect alone these taxes and charges. The municipalities, which have not taken up the administration of these taxes and charges by 2005, shall pay to the government to carry out this activity. But some experts are afraid that many municipalities are not prepared to collect alone the local taxes and charges, because they might encounter problems in calculating the waste collection charge and some other local taxes. The new tax collection treatment implies that municipal officials should be engaged in sending notices of the payable waste collection charge and inhabitant house duty and in issuing real estate tax valuation certificates to individuals.

As early as 2002 two municipalities in the region of Burgas (Pomorie and Primorsko) began to administer alone the local charges and taxes. Since the beginning of 2004 another three municipalities in the same region will collect alone the local charges and taxes. The implementation of this project is part of the tax administration reform, which should be completed by 2006 before Bulgaria's accession to the EU. The project also envisages establishment of an Integrated Revenues Agency and its value is EUR 63 million. Within this project the corresponding municipalities will get computer systems, software, databases and qualified personnel who will provide expert and methodological assistance to the local government.

The implementation of **projects resulting in improved quality of municipal services for the business and the people** continued. The Investment in Business Incubators in Industrial Decline Regions Project within the PHARE Program, implemented in Vratza, Montana, Mezdra, Madan, Kardzhali and Belogradchik, is one of these projects. The maximum budget for each region is EUR 140 - 150 thousand. The total value of the project, which will be actively implemented in 2004 and 2005, is EUR 900 thousand.

A new important PHARE Program instrument to be implemented since 2004 was announced at the end of 2003 – the **External Borders Initiative**, the objective of which is to improve the standard of living in border regions, to develop trans-border cooperation and to support the activity in the economy,

culture, tourism, and environment sectors. The initiative covers Bulgaria, Serbia and Montenegro, Macedonia and Turkey, which will be external borders of the EU in the future. The support for the Bulgarian projects within this program amounts to EUR 4.12 million, with national co-financing of 10 or 25 per cent required.



## THE BULGARIAN ECONOMY IN 2003

### Center for Economic Development Team

*In 2003, the Bulgarian economy continued its generally positive development characteristic of the past few years. A relatively high growth of the GDP was achieved together with an improvement of the performance indicators in a number of economic sectors in an environment of preserved macroeconomic stability. Government's commitments for improved economic policy and the positive results in some policy areas are among the factors determining some improvement of the business climate in the country and of unemployment, inflation and government debt indicators.*

*Some policy areas, however, such as investment policy, transport, and health care, registered delay or even lack of development and reforms. Economic growth remains insufficient for a significant change in incomes and employment. Competitiveness is improving at sector and company level but Bulgaria is still insufficiently prepared for the economic implications of a prospective EU membership.*

A typical feature of the entire year is that value added of industrial sector is increasing at higher rates compared to the value added of services, with the opposite trend observed in 2002. In the third quarter of 2003, the value added of industry increased by 8.4 per cent on an annual basis, that of services increased by 4.2 per cent, and the contribution of the sectors industry and services in the **GDP growth** was 2 percentage points each. In the event that there are no alterations in the GDP growth data for the first three quarters of 2003 and with an estimated growth for the fourth quarter of about 4.3 per cent, total economic growth for 2003 can be projected at **4.2 per cent**.

The first ten months of 2003 are characterized by a relatively smooth **price dynamics** only violated in November and December by a sharper increase of the consumer prices of several groups of foods (bread, meat, fresh vegetables), which resulted in total inflation rate at year end of 5.6 per cent against December 2002. However, the more shallow and smooth price dynamics since the beginning of 2003 compared to 2002 resulted in a lower average annual inflation rate for 2003 (2.3 per cent against 5.8 per cent for 2002).

Despite some increase of **unemployment** at year end, which is a typical seasonal phenomenon for the period since 1991, this indicator registers a stable downward trend in the long run. The number of unemployed has decreased by 100,000 people, or 17 per cent, compared to December 2002, and that is the largest absolute and relative decrease observed in the month of December compared to the last three years.

In 2003, the **Current Account deficit**, amounting to USD 1 648 m (8.7 per cent of GDP), exceeds more than twice the deficit for 2002 (USD 712.6 m or 4.6 per cent of GDP, respectively). The aggravated Current Account is accounted for in the first place by the deteriorated trade balance (94.0 per cent), which is determined by the leading growth of import stimulated mainly by the growth of domestic lending. The negative contribution of the (net) Income item for the aggravated Current Account (19 per cent) is realized in the first half of the year and can be explained mainly with the increasing debt of the private sector, with operations for restructuring of the government debt, with payment of dividends. The total annual contribution of services for the changes in the Current Account is negative (2.7 per cent of the annual aggravation). The improvement of the (net) Current Transfers item contributed by 15 per cent for the compensation of the negative effect of the trade balance and net income.

The increase of the BNB currency reserves at year end predetermines the improved BNB Currency Reserve/Import of Goods and Non-Factor Services ratio (6.5 months) compared to December 2002 (6.1 months).

In the context of the slow recovery of world economy, the growth of Bulgaria's **foreign trade** in 2003 can be regarded as a positive phenomenon. Such an increase in trade (30.7 per cent for exports and 35.9 per cent of imports in USD) has not been observed in the past few years. Moreover, the values of exports and imports are the highest since 1989. Expressed in Bulgarian leva (eliminating the effect of the cheaper dollar), the increase is 9.9 per cent and 14.1 per cent, respectively. This indicates a better working economy. However, a larger negative balance is also viewed as a serious threat to the financial system, the sustainability of the economy as a whole and its sustainable development in the future.

Increased consumption is not the only factor for the substantial growth of imports and the negative trade balance. Industrial production registers a stable growth which results in increased import of investment goods and raw materials at rates above the general (41.6 per cent and 66.6 per cent, respectively). This import accounts for 1/3 of total imports and is not a threat to local production. The data indicate that there is no substantial increase in consumption compared to the previous year. The relatively stable incomes and the growth in consumer loans stimulate consumption but its increase is too small (mainly in quantitative terms and not in real value). All this indicates that the increase in the import of consumer goods is largely a result of officializing illegal import and not of real increase in the quantities. If we assume that the main channels have already been blocked or at least limited, such an increase of import should not be observed in 2004. In this sense, the import dynamics in 2004 will indicate whether there are grounds for

concerns and a real threat for the current account and the balance of payments.

Based on the geographical orientation of trade and most of all on the increasing share of the EU (57 per cent in exports and 50 per cent in imports), it may be concluded that there is no serious threat to the trade balance as in the pre-accession period (and after the new countries' accession to the EU) the Bulgarian economy will still rely on its established positions on the European market and on its competitiveness based on lower production costs. It is precisely competitiveness that helped increase exports in this direction even in the period of stagnation of the European economy and of the consumption on the common European market.

The big trade deficit is largely compensated by the inflow of foreign investments. According to preliminary data, the total **foreign direct investment** for 2003 is estimated at USD 1 361 b. It is quite possible that, following some revisions, the result be considerably higher (up to USD 2 b). This is the largest volume of foreign direct investment since 1992. With the comparatively small volume of funds from privatization transactions (USD 370 m, about 27 per cent) and from other transactions (approximately the same amount), the largest share is that of other capital attracted (42 per cent), accounting for revenue from different types of loans. It registered a growth of 2.5 times compared to the previous year. These are production loans for joint ventures, which have to be repaid. Overall, the foreign companies represented in the country (or companies with foreign participation) are already beyond the period of establishment and are developing their activity providing good basis to attract a higher number of domestic suppliers. Despite that, however, the economy still suffers from an acute lack of green investments and of new investments by strategic investors. Government's commitments for changes in the investment policy geared towards attracting more capital in the economy are before all related to the implementation of new criteria aimed at promoting foreign as well as Bulgarian investments and at eliminating the bureaucratic barriers. The objective is to turn efficient administrative services into an additional advantage of the Bulgarian economy together with qualified, low-paid labor.

In the first three quarters of 2003, the value of the **Estat Index of business climate in Bulgaria** registered a slight upward trend. In October, this index reached its peak value since April 2002. In January 2004, a slight decrease of the index value was observed. The main reasons for that are mainly related to certain negative changes in the investment attitudes of the business and to seasonal fluctuations in the assessments of the condition of economic entities.

As a whole, according to the interviewed entrepreneurs, the business climate in the country may still be characterized as rather neutral, registering an unstable trend towards

improvement. A positive development is the increase registered by certain assessments about the business environment. A number of indicators reached their highest values since the beginning of the surveys in 2002. These indicators are mainly start-up of a business and effect of administrative barriers. The percentage of entrepreneurs who do not consider administrative obstacles to be a major problem in the start-up and operation of companies is increasing. Probably, it is the measures oriented towards reduction of regulatory regimes that have a positive effect on the business attitude. At the end of 2003, the new Act on Restricting Administrative Regulation and Administrative Control on Economic Activity was enacted.

Another positive fact is the change in the attitude towards the public administration. January 2004 witnessed the lowest share of interviewed stating that they are ready to pay an additional amount just to avoid any difficulties in the contact with the public administration. The assessment of the regulation of market competition is another indicator registering improved attitude compared to the previous survey and against the whole previous year.

The attitude of the business towards the tax environment continues to improve. A sustainable positive trend is observed in the assessments of the business about the sustainability and reliability of the banking system. Although the overall attitude towards Government's policy for business promotion remains negative, assessments of Government's legislative initiative register slight improvement as well. According to the business, however, major difficulties are a result of the absence of efficient and consistent implementation of the legislation. This confirms the fact that the harmonization of the legislation with the *acquis communautaire* is successful but the application of legislation constitutes a major weakness.

There is also a need of a more active policy for promotion of entrepreneurship and the use of high technologies in the business. There are still some doubts regarding the transparency of bids organized under the Public Procurement Act. The greatest concern, however, is the decline in the share of managers who believe that the harmonization of the Bulgarian legislation leads to improvement of the business environment in the country. Last year, the assessments of this indicator were rather variable. This may signal absence of a consistent explanatory campaign and sufficient information about the advantages and difficulties related to Bulgaria's EU accession.

A number of public forums on the problems of entrepreneurs were organized throughout 2003. The purpose of these forums was to facilitate the dialogue between the Government and the business. However, these forums did not yield specific practical solutions which could help to improve the institutional framework. Some development along these lines was observed during the second half of the year after

the changes in the Government's economic team. A number of legislative changes regarding small and medium-sized enterprises were proposed. Substantial improvements were made in the structure and functions of the Ministry of Economy (MoE). The MoE is expected to turn into the main generator and coordinator of the economic policy and the policy for promotion of entrepreneurship provided the amendments to the Act on Small and Medium-Sized Enterprises are adopted on second reading by the Parliament. Currently, MoE's work with the business on the **requirements to the latter resulting from the future EU membership** is still lagging behind. Less than 36 months remain till the expected EU membership and entrepreneurs do not have yet adequate information as to how this will influence their business. The requirements-promoting process is a bilateral one but the MoE should play the leading part in launching information campaigns about the different negotiation chapters. Government's Communication Strategy for Bulgaria's EU Membership announced in early 2004 was a substantial step forward in this respect. In 2004 further improvement of the institutional framework for development of entrepreneurship can be expected after the adoption of the set of laws having a direct effect on the activity of small and medium-sized enterprises<sup>27</sup> and on the investment climate, especially upon their implementation in practice.

The **access of the business to financing** registered improvement throughout the whole 2003. This resulted in a gradual decrease of one of the most important limitations to the start-up and doing business in Bulgaria. Due to the stable decrease of interest rates on the international markets, Bulgarian banks brought large amounts of savings back to the country, which provided additional incentives for granting loans. This increased competition among banks and they introduced relieved requirements and reduced interest rates on loans up to a certain level. The result is an increase of newly negotiated loans for the business by 38 per cent (in absolute terms) compared to 2002. This forced the BNB to introduce certain restrictions on commercial banks' lending expansion. As a result, slower lending growth rates can be expected in 2004. At the same time, however, a continued upward trend of loans in absolute terms may be expected. In addition to this conclusion, it is worth mentioning the new credit lines that banks agreed on for loans to small and medium-sized enterprises, with the larger amount negotiated under EU's pre-accession programs and the financial framework for Bulgaria. All these factors will probably lead to further increase of economic investments by Bulgarian entrepreneurs.

As 2003 was the most successful year since the start of transition in terms of attracted foreign **investments**, the amendments to the Foreign Investment Act proposed by the MoE in the last quarter of the year will further open the economic policy to economy's needs of more investment. After adoption of the amendments,

new record levels may be expected in 2004 in terms of green investments in the economy. The methods planned for sale of companies within the Bulgartabac Holding system and the other large state-owned enterprises have a potential for a successful year and for investment from privatization.

**Different measures to reduce administrative barriers, improve public procurement procedures, promote fair market competition and improve bankruptcy procedures were introduced in 2003. A number of steps were taken to increase the efficiency of the judiciary system and to combat corruption.** Regardless of that, entrepreneurs do not see yet any substantial improvement in the business environment. It seems that the economic policy does not pay enough attention to institutional incentives for promoting entrepreneurship: most changes in the legislation throughout 2003 may be given a positive assessment but they alone do not mean an improved environment for start-up and doing business. This is mainly due to the fact that in the area of implementation of the legislation, there are still substantial deficiencies at all administration levels, at all hierarchical levels and in all regions in the country.

2003 registered continued introduction of **European norms and standards in production and trade** which had negative effect in a short-term perspective on some sectors such as food industry for example. The gradual implementation of these standards is expected to increase the competitiveness of Bulgarian companies on the global market. Progress is also observed in the area of promoting **trade in Southeast Europe**. The series of bilateral agreements on the elimination of trade constraints between the countries in the region, signed in Rome, will create additional niches for export-oriented Bulgarian companies that are still unable to meet the competitive pressure of the market forces on the common European market. An increase of the volume of trade with countries in the region may be expected in 2004. The export of Bulgarian goods and services will grow faster than import due to the increased competitive advantages of the Bulgarian companies.

In the area of **privatization**, the general impression that the Privatization Agency is not efficient was confirmed and that generated new ideas for substantial amendments to its status. If the proposals for amendments to the privatization legislation are adopted in 2004, they will have a positive effect on the future privatization processes. The 2003 work plan of the Privatization Agency sets minimum goals, but even these were not achieved. Only 61.4 per cent of the planned majority shares were sold, less than half of the detached parts intended for privatization and about one-fourth of the planned minority shares in private companies were sold. Revenues from privatization also fail to reach the planned levels. The stagnation in the privatization of large state-owned companies continued and the expectations in this area also proved higher than actual achievements. Nevertheless, the new strategy for sale of Bulgartabac Holding and its companies, adopted at the

<sup>27</sup> Amendments and Supplements to the Act on SMEs', Act on Promotion of Investment in SME's, and Amendments and Supplements to the Foreign Investment Act.



end of the year, the interest expressed by international tobacco and tobacco product market leaders to this new privatization scheme, and the projections for completed privatization of the Bulgarian Telecommunications Company in 2004, give grounds for new positive expectations about the “large privatization” in 2004. There are also positive expectations for the other areas and elements of the privatization process.

The major events in the area of **public finance** in 2003 include the good execution of the consolidated fiscal program, the balanced budget achieved for the first time since 1999, the operations with the fiscal reserve, the continuing decrease of the debt/GDP ratio, the improved credit rating of Bulgaria, the adoption of the 2004 budget and the amendments to the tax laws.

The **balanced budget** achieved during the year is a sign of stability in public finance. On the other hand, with a deficit of BGN 262.8 m planned in the budget, the small surplus realized was a result of the substantial reserves available in the budget and of the conservative approach to revenue planning. Another practice working in the same direction is the postponing of certain expenditures for the end of the year while their realization is dependent on the good execution of the revenue part of the budget. In 2003, some of the expenditure items postponed until the end of the year were again the funds for financing the National Health Insurance Fund, the unpaid amounts for municipal state-delegated activities, the Christmas supplements to pensions, and the “thirteenth” salary for state employees. In 2004, an additional amount of up to BGN 500 m for funding infrastructure projects will be added to these expenditures. The spending of these resources is planned for the second half of the year provided that budget revenues are well executed.

The depositing of BGN 185 m from the **fiscal reserve** in five Bulgarian banks in June, prompted serious public debate on the transparency and the macroeconomic effects of this operation (increased money supply and inflationary pressure) which continued during the whole year. Following a substantial delay and after the negative reaction of the International Monetary Fund (IMF), a draft Supplemental Act to the State Budget Composition Act was submitted for deliberation in the National Assembly. The draft envisages that the National Assembly will determine the minimum required reserve in accordance with the public character of the funds.

In 2003, total **government and government-guaranteed debt** decreased by BGN 1 670 m recalculated at BNB's central exchange rates of the lev as of December 31, 2003. The debt/GDP ratio decreased from 56 per cent at the end of 2002 to 47.8 per cent at the end of December 2003. The decrease of the total amount of debt (in absolute and relative terms) is entirely due to the decrease in the foreign debt. At the same time, the foreign debt structure reveals a steady trend towards increase

of the share of the euro-denominated debt at the expense of the debt denominated in US dollars. There is a gradual increase of the share of floating interest debt. The domestic debt is still increasing. The share of government securities issued to finance the budget deficit is increasing.

After Standard & Poor's and Moody's raised Bulgaria's long-term **credit rating** in domestic and foreign currency in the second quarter of the year, in the following quarter Japan Credit Rating Agency (JCRA) and Fitch Ratings also revised their ratings in a positive direction. Upgraded credit ratings reflect the agencies' positive evaluation of Bulgaria's stable macroeconomic policy and results supported by the currency board and the country's ambitions for EU membership. These two factors are expected to ensure a rapid decrease of the country's domestic and foreign debt ratios.

The 2004 state budget and the amendments to the tax legislation were adopted at the end of the year. The **2004 budget** continues the trend observed over the past several years towards an increase of the funds redistributed through the revenue and expenditure part of the budget in absolute terms and as a share of GDP. One of the main reasons for that was the delay of the reforms in the public sector and the increasing number of persons employed in the budget sector. Priority in the area of expenditures was given to areas requiring further restructuring, i.e. education, health care, judicial system, infrastructure. At the same time, the question how efficient increased expenditures will be in the absence of elaborated mechanisms for distribution and spending of the funds is still pending. A typical example are the funds allocated for infrastructure projects, up to BGN 500 m, included in the Financing part (in other words, outside the expenditure part of the budget). There is still lack of clarity as to whether and how these funds will be spent. The main criticism is related to the absence of transparency and the macroeconomic effects of that measure.

The purpose of the amendments to the **tax laws** is above all to create favorable conditions for business development. That is why the decrease of the tax burden is more substantial for entities subject to taxation under the Corporate Income Tax Act compared to persons liable under the Personal Income Taxation Act. In addition to the decrease of corporate income tax by 4 percentage points (from 23.5 per cent to 19.5 per cent), there are also other facts that are substantial for the business such as the equalization of the VAT registration threshold with the ceiling on annual turnover subject to presumptive taxation (BGN 50,000), the relieved tax regime for certain types of expenses, etc. One substantial change that was not included in the latest amendments was the introduction of family taxation that would guarantee a higher level of fairness in taxation and equal standing for all tax liable entities.

The past 2003 built on and reinforced the positive results in the implementation of a modern and active **social policy**,



the foundation of which was laid in 2002. With the necessary continuity in the work of the Ministry of Labor and Social Policy teams, the Government has dealt successfully with the development of vital laws and strategic documents in the social area. The Government efficiently implemented its specific programs and projects focused on solving the problem with unemployment and on curbing poverty. Major efforts were focused on employment, policy towards underprivileged individuals, improvement of the labor legislation and the social dialogue. Currently, Bulgaria's social legislation as a whole is harmonized with the EU social laws. It is necessary, however, to focus on its prompt and efficient implementation as well. The rates of restructuring and modernization of two areas vital for the development of Bulgaria's human resources in Bulgaria – health care and education – are still unsatisfactory and remain part of social policy priorities. The year was marked by record low unemployment rates (12 – 13 per cent) in comparison with all other years of the transition and with extensive periods of growth of the real incomes of Bulgarians, although at uneven rates.

The positive results in this area are mainly due to the large-scale implementation of subsidized **employment** programs, i.e. the National Program *From Social Assistance to Employment*. In 2003, a total of 103 505 long-term unemployed were given a job under this program. The program is operating successfully in many Bulgarian municipalities. Its results are substantial both in terms of created jobs and in terms of a real improvement of the living environment. Although sharply criticized at times, the program has a strong social intensity and is, in its nature, a social integration program for long-term unemployed who are thus given a chance to regain their working habits, to become literate and acquire new qualifications, and to return to the labor market eventually.

The effect of a number of other programs is also worth mentioning. The main advantage of such programs is that they are specifically designed to support the job finding process of specific risk social groups. Together with that, employment is increasing as a result of job openings in the private sector based on positive economic dynamics. Incentives to employers provided under the latest amendments to the Employment Promotion Act have a substantial contribution thereto. Although these measures are not always successfully implemented, i.e. zero profits tax rate for high unemployment areas, overall the labor market is increasing its dynamics and the creation of jobs is promoted. All these measures and projects in the labor market area are a good basis for reducing unemployment and increasing employment over the short-term. Together with that, they should also pursue longer-term goals so that the quantitative and qualitative parameters of employment in Bulgaria could guarantee the attainment of the economic and social criteria for the country's EU membership. This is especially true for the level of qualification of the workforce and its adaptability to the changing economic situation.

Despite the substantial achievements in 2003, due to the concentration of unemployment in certain geographic regions and/or social groups, it is still too early to state that the problem with structural unemployment in Bulgaria has been permanently overcome.

The expectations for 2004 are that the Government will continue to provide employment for more than 100 000 people under subsidized employment programs and to finance training and vocational qualification for the unemployed. Long-term unemployed, young people without any work experience and occupation, and people with disabilities are the target groups of the active employment policy. Although the private sector has not yet turned into a powerful generator of new jobs, a substantial aggravation of the employment levels should not be expected.

According to data about salaries and household budgets from the National Statistical Institute, the past 2003 witnessed an increase of the **incomes** of Bulgarians in nominal and real terms. The major factors for this positive effect include: continuing low inflation rate, positive economic dynamics, employment programs, and differentiated higher levels of certain social benefits. The relatively stable levels of income and the growth of consumer loans encouraged the households to consume more basic consumer goods in qualitative and quantitative terms compared to 2002. Yet the fourth quarter data do not give grounds to say that this trend will be preserved in 2004 as well.

At the same time, the results from the NSI's regular surveys of consumers' confidence become more and more pessimistic. The negative twist in consumers' assessments and expectations in 2003 regarding the general economic situation in the country, the financial situation of households, inflation and unemployment rates, is a signal of setbacks in the economic and social policies.

Although difficult to capture in terms of size, but nevertheless inevitable, additional payments for education and health care should also be taken into consideration when estimating the Bulgarians' standard of living. In this context, the planned increase of electricity and heat prices and the increase of excise duties on fuels in 2004 will create conditions for a higher level of social tension, insignificant increase or stagnation of consumption and, eventually, a continuously low standard of living for large groups of Bulgarians.

A substantial achievement of social policy in 2003 was the improvement of the **social assistance** principles and mechanisms and its efficiency with respect to the most vulnerable social groups. The access to social benefits was enlarged for elderly people living alone, single parents, people with disabilities and other specific categories of people who require a differentiated approach to their problems. In

productive cooperation with all institutions and organizations concerned, the Ministry of Labor and Social Policy (MLSP) has prepared and adopted a comprehensive package of documents presenting the policy for people with disabilities, antipoverty and social isolation, and protection of homeless children.

When assessing social assistance measures implemented in 2003, it should be emphasized that this is not a campaign or a single effort. It is a logical conclusion of a process whose start was given at an earlier stage. From now on the challenge will be to effectively implement a large number of strategic and programming documents and to complete them with new and modern forms of social services. The success of the government policy in this field will be dependable on the efficient efforts of all institutions and the media to overcome public reticence, that of employers in the first place, towards the abilities and skills of the disabled people.

In 2003, there were isolated cases of **social discontent** in individual sectors and enterprises. The protestors' requests were most frequently related to delays in the payment of salaries and social benefits, delay in the conclusion of collective bargaining agreements, and absence of social adaptation programs in case of lay-offs related to forthcoming privatization. Nevertheless, none of these cases generated any serious social conflicts. Social dialogue and social partnership mechanisms are established on national level, as well as on sector and enterprise level.

In 2003, Government's policy in the area of **social insurance** can be characterized as comparatively active and effective. Nearly half a year after the first reading at the National Assembly on December 20, 2002, the new Social Insurance Code (SIC) was passed at second reading at the end of June 2003. Certain provisions were returned for revision by the President of Bulgaria. The new SIC created a unified, improved legal system regulating public relations in the area of social insurance. The most debatable issue was the relation or the lack thereof, between the pension insurance company and the custodian bank. Eventually, the new Code incorporated the principles adopted in the international practices.

The change of pension fund issue was settled at a later stage at the end of the year with the adoption of Ordinance No 3 of the Financial Supervision Commission (FSC). Experts project that not more than 5 – 10 per cent of all pension fund members will change their participation. The underpinning campaign started on January 1, 2004 and it is expected to allow the smaller funds to increase their market share. A substantial aspect of the new SIC, which will make fund members active participants in the management of their funds, is the provision requiring individual account savings to be measured in units in addition to absolute amounts. This requirement will come into effect on July 1, 2004. Thus the value of a unit will provide information as to how efficient is the investment of the fund member's savings.

The two new requirements to the business implemented in early 2003 by the MLSP and the National Social Security Institute (NSSI) have a positive effect on the collection of social security contributions and on curbing shadow economy. The introduction of minimum social insurance thresholds by sectors and by professions and the mandatory registration of labor contracts at the NSSI resulted in collection of additional BGN 250 m of revenues for the social security budget in the first nine months of 2003. This fact created some optimistic expectations for solving the problem with the deficit of the Pensions Fund which would allow a decrease of the social insurance burden and an increase of pensions.

On the other hand, the 2004 Social Security Budget Act adopted in December 2003, which fixed the maximum pension amount at BGN 420, and which provides for a greater amount of additional subsidies from the central republican budget to cover the deficit (about BGN 576 m for 2004 compared to about BGN 383 m for 2003) does not give grounds to expect a general decrease of the social insurance burden in the near future.

The increase of the universal pension fund contribution from 2 to 3 per cent from January 1, 2004 for persons born after December 31, 1959, is evaluated as a motivating factor for the participation of young people in the social insurance system and as an opportunity for the private pension funds to use their experience and to invest the accumulated funds more efficiently. The problem related to payment of the first days of sick leaves by the employers was solved only partially. Both in 2003 and in 2004, government employees will be again in a privileged position compared to workers employed under labor contracts as the Government will continue to pay their social security and supplementary mandatory universal pension contributions. The fact that contributions for temporary disability or pregnancy and birth-giving will still be paid at the expense of the insurer or the self-employed caused significant discontent of the business.

The new Social Insurance Agreements signed in 2003 with Macedonia, Croatia, Serbia and Montenegro and the Agreement for Export of Social Insurance Payments with the Kingdom of the Netherlands, approved by the government, are a step ahead towards achieving better coordination between the Bulgarian social insurance system and the systems in the EU Member States and candidate countries, which is one of the requirements of the *acquis communautaire*.

The acquisition of the Bulgarian Pension Insurance Company by Doverie Pension Insurance Company in 2003 set the beginning of the consolidation process in the Bulgarian pension market. It is expected that this process will continue to unfold and the pension insurance companies will become major players on the capital market. The pension license issued by the FSC to DZI – Pension Insurance, introduced a new player on the pension market. The higher competition among pension insurance companies as a result of the greater number of participants on

the market and the possibility for switching between pension funds from January 1, 2004, is expected to improve the diversity and quality of the pension services offered and to guarantee a higher return on the investment of pension savings. The supplementary pension insurance companies claimed a full tax preference of voluntary contributions, which is a good incentive for the development of the voluntary pension insurance system. Eventually, a ceiling on contributions was introduced from the beginning of 2003 whereby individuals may deduct up to 10 per cent of their income before taxation if they make third pension, voluntary health and unemployment insurance contributions.

In one year the participants in all supplementary pension insurance funds have increased by more than 26 per cent. The greatest increase is registered with universal pension funds, by more than 38 per cent, which is mainly due to the measures taken by the Government to curb the shadow economy and to solve the problems with unemployment. In one year, the amount of net assets has grown by more than 50 per cent. The growth of universal pension fund assets is more than 173 per cent. According to the estimates of the Bulgarian Association of Supplementary Pension Insurance Companies for 2004, the amount accrued in all pension funds will reach BGN 685 m. That, however, will require a more efficient investment activity by the pension insurance companies. Dovereie PIC has managed to attract the greatest number of participants in all three types of pension funds in 2003, while Allianz Bulgaria AD has the largest market share in terms of pension assets. Pension funds continue to invest assets mainly in government-issued or government-guaranteed securities and in bank deposits. It is important to note that in the last quarter of 2003, there was a substantial increase in the share of investment in mortgage bonds, which is an indicator of the increasing diversification of the funds' portfolios.

As regards **health policy**, 2003 came to show that the tendency to have the National Framework Agreement (NFA) signed and taking effect with delay is preserved. Hoping that the 2004 NFA would come into effect on January 1, 2004, and would achieve a better balance between the interests of the insured persons and those of medical care providers, the Ministry of Health (MoH) presented as early as September its new recommendations on the major principles that had to be included in the new contract such as raising the criteria for in-patient care standards, elimination of the regional segregation of hospitals, introduction of clinical paths for a specific group of diseases and introduction of mandatory electronic data exchange in in-patient care. A positive assessment is given to the initiative of the MoH and the NHIF to continue the reforms in in-patient care in order to guarantee more efficient functioning of the entire health care system. In August 2003, MoH and NHIF signed a protocol for division of the commitments of the two institutions for a stage-by-stage change of financing system of in-patient care in Bulgaria. The document is a "road map" for

in-patient care reforms, which offers a medium-term strategy for its implementation in the period 2003 – 2010.

The mechanism for funding medical institutions in 2004 caused serious disagreements between doctors and the health fund as early as the beginning of the negotiations on the new framework agreement. The Association of Private Medical Institutions in Bulgaria also expressed its discontent with the new mechanism. The Association insisted on the introduction of a regime of equality in the funding of state-owned, municipal and private medical institutions. For the first time, medical institutions start the year with minimum debts. In the opinion of experts, however, due to the delayed signing of the 2004 NFA, it is expected that in the beginning of 2004 medical institutions will continue to accrue debt. A possible solution to the problem may be sought in the more efficient management of medical institutions. The issue of privatization of medical institutions, which is an integral part of the restructuring of this sector, remained unsolved in 2003 as well.

The first Bulgarian Positive List of Medicines, which is a major instrument for implementation of the national medicines policy, created serious tension between Bulgarian and foreign pharmaceutical manufacturers. The reason for that is the expected decrease of sales of foreign pharmaceutical manufacturers in 2004 which account for 66 per cent in 2003. The problem with insufficient funds for medicines planned in the 2003 NHIF budget forced the Fund to request updating of its budget from the National Assembly in 2003, which happens for the first time in the history of the Fund. Despite the measures taken to stabilize monthly expenditures for medicines at BGN 19 – 20 m and the higher amount planned for home treatment in the 2004 NHIF budget (by 45.3 per cent more in 2004 compared to the voted 2003 NHIF budget or by 12 per cent more in 2004 compared to the updated 2003 NHIF budget), it is essential to note that the lack of integrated information system in health care is a serious threat for the funds for medicines to prove insufficient again.

In 2003, there was an increased interest in voluntary health insurance on behalf of insurance companies. Four new companies were licensed to perform voluntary health insurance, Bulstrad – Health Insurance AD, Health Insurance Shareholding Company DZI AD, Medico 21 Health Insurance Fund AD, and Bulgarian Health Insurance Fund AD. This indicates that this market is still underdeveloped and the prospects for its development are rather good.

The frequent legislative changes in the sphere of health insurance and the insufficient level of awareness of changes on behalf of both insured persons and medical service providers cause insecurity and lack of trust in the health reform. Changes should be coordinated with all stakeholders in the health care sector and an efficient mechanism for coordination and cooperation should be created.

Environmental policy in 2003 can be characterized as successful in several aspects. Bulgaria has completed the negotiations with the EU on Chapter 22 *Environment*. As a result of that, the country has not only achieved progress in the overall negotiations process but it could also report a high degree of harmonization of the national legislation with the EU directives in almost all environmental sectors (excluding legislation in the area of noise and genetically modified organisms). Special attention should be paid to the progress in the area of waste and water management (an entirely new Waste Management Act was adopted and municipal advisory structures responsible for river basin management on the territory of the country were established in accordance with the European Water Framework Directive 2000/60/EU and the Wastewater Treatment Directive).

As for market economic instruments related to environmental policy, a priority in the practice of companies during the year was given to voluntary mechanisms such as eco-marking (a National Eco-Marking Scheme has been approved) and certification of goods and services. The implementation of environmental standards is not an exception any more, nor is it a characteristic of companies with foreign participation. The first integrated international certificate in the country is already a fact in the area of risk heavy industry, based on ISO 9001:2000 for quality assurance, ISO 14 000:1996 for environment management and OHASAS 18001:1999 for health and safety at work. This certificate was awarded to Asarel-Medet AD. The development and application of environmental programs is part of the business strategy of most Bulgarian companies.

The principles of sustainable development and environment-friendly use of natural resources, improvement of the characteristics of soils, improvement of the quality of agricultural produce and the characteristics of the forestry fund in the country have been implemented successfully with respect to the regulation of activities in the area of agriculture and forestry. During the year, a national Agro-Environmental Program was developed as a result of the joint activities of the Ministry of Environment and Waters (MoEW) and the Ministry of Agriculture and Forestry (MoAF). This program will be applied after Bulgaria's EU accession. The recovery and sustainable development of the Bulgarian private, municipal and state-owned forest resources, and the conservation of biodiversity, at the same time, is the main goal of the Bulgaria – Development of the Forestry Sector Project whose ultimate goal is the development of a national forestry policy and strategy.

A number of principally new approaches were adopted in the area of energy efficiency. The newly adopted Energy Act regulates the production of energy from renewable energy sources, the use of biomass and the use of wind energy. The forthcoming amendments to the Act on Waters are planned to regulate the use of non-traditional sources of energy such as thermal waters for example.

The main problems outlined in 2003, which are expected to influence the priorities of environmental policy in 2004, may be summarized in several major areas. An assessment of the efficiency of the administrative structure at central and regional level is necessary in order to formulate clear management goals. This would also allow the administrative capacity of the central and regional units of the MoEW to control the implementation of decisions and procedures adopted and to ensure a procedure for appealing of administrative statements related to environmental protection issues and to natural resource management. This assessment should be available to the general public and to the business.

An expansion of the cooperation with academic and technical circles is necessary as well as strengthening of their role in the support of practical environmental management, together with an expansion of the MoEW databases, harmonization of the practices of environmental protection controlling bodies in the whole country, ensuring up-to-date, sufficient information related to the planning of companies' production activities and the implementation of their business strategies. Introduction of economic mechanisms for promotion of investment activity is required in relation to improvement of the environmental situation in the country, including environmental investments made by private donors at local and regional level. Improvement of the public access to information regarding environmental inspections, controlling procedures, plans and programs at national, regional and local level is required. The role of local governance needs strengthening in the decision making process and the role of local government needs strengthening in the procedure for environmental impact assessment to ensure a higher level of responsibility and clearer definition of the hierarchy of responsibilities in cases of appeal. Equal control is needed for all environmental components and for the development of programs for pollution prevention.

The credit expansion in the **banking system** was the hottest topic in 2003. The annual growth rate of bank receivables on credits to the non-government sector amounted to 48.8 per cent and the annual growth of newly negotiated loans was 38 per cent. The annual growth rate in loans exceeded the growth of bank assets, 19 per cent, and the growth of deposits, 20 per cent. Despite the increase of loans, the condition of banks remains stable, with excellent capital adequacy and liquidity indicators and well-functioning banking supervision. The quality of the loan portfolio is also good. At the end of 2002, 94.47 per cent of all categories of loans were classified as performing, whereas at the end of September 2003 94.05 per cent were classified as performing.

January 1, 2003, marked the introduction of the International Accounting Standards for banks. That imposed a number of changes in the format and structure of their balance sheets and profit and loss accounts. As of April, the Banking Supervision Department at BNB altered the grouping of commercial banks.



The ranking of banks in the groups depends on the amount of their assets. Group I always comprises ten banks, Group II, the rest of the banks, and Group III includes branches of foreign banks in Bulgaria. During the year, the BNB issued a license for banking activity to a new bank, West-East Bank AD. Thus, currently, there are 35 banks in Bulgaria.

The liquidity crisis on the lev market in mid-April was one of the interesting events during the year. This crisis (commented as being the greatest in our banking system since the establishment of the currency board arrangement), was overcome after the Ministry of Finance organized an auction for redemption of securities. With that, a total of BGN 25 m was allocated to the banks at an average rate of return of about 11 per cent. There were some concerns that only specific banks were favored by the cheaper resource but that was firmly denied by the MoF. As for the reason and nature of the crisis, it was probably due to poor management and estimation of cash flows by the banks; or maybe by the MoF too.

The possibility of having such a crisis repeated was to a great extent eliminated in June when the BNB allowed commercial banks to validate their accounts in EURO with the BNB with a value date on the same working day (and with the same value date to sell EURO for levs to the BNB). In addition, the RINGS system (real time gross settlement system) was successfully launched in June and now all system-essential payments go through it. The RINGS system is compatible with the European Central Bank payment system TARGET and will allow processing of international payments and payments in EURO after Bulgaria's EU accession.

The year will also be remembered with the completed privatization of banks in Bulgaria. The sale of DSK Bank AD was finalized in the fall. After that sale, more than 97 per cent of the banking system assets are owned by private entities and foreign banks and investors control over 85 per cent of bank assets (calculated per assets through the end of 2002). Encouragement Bank AD and Municipal Bank AD are the last two banks with state-owned and municipal, respectively, control on the capital.

The delayed appointment of a new governor and deputy governor (and director of the Issue Department) of the BNB turned into another major event for the sector in 2003. Although the term of the former governor expired in June and the deputy governor (and director of the Issue Department) resigned in the beginning of the year, a new governor and deputy governor of the BNB were appointed by the National Assembly in October. Most discussions and experts' assessments were focused on BNB's independence, the political reasons for the appointment, and the role of the BNB in the fiscal reserve management which turned into a major issue after MoF's operation for depositing part of the reserve in commercial banks in June.

Another event that was the subject of many discussions over the past several months was the procedure for privatization of the national card operator *Borica AD*. The BNB appointed a valuator of *Borica AD* and the forthcoming sale raised the interest of a number of financial institutions in the country and of potential foreign investors as well. By the end of the year there was no specific action regarding the privatization but at a later stage the Association of Commercial Banks made a proposal to the manager of the company to develop a long-term strategy for its development with the participation of an independent external consultant. The scheme for the sale of *Borica AD* should be a key element of this strategy.

The discussion of the possible threats arising from the increased lending activity of banks dominated the second half of the year. The quality of loan portfolios and the potential stability of the banking system were the major topics of discussion (mainly after the visit of the IMF mission to Bulgaria). Attention was also focused on the link between the growth of imports, the current account deficit, respectively, and the lending expansion. The IMF representatives insisted very much on the need for stricter control on banks' lending activity. The BNB accepted IMF's arguments about the need to hold up the growth of credits to private enterprises and households. The measures taken in this respect included on the first place the amendment to Ordinance No 9 of the BNB. The Ordinance was amended one more time in the beginning of 2004 and that, together with other measures announced by the BNB (i.e. launching of the unified credit register), allowed the Bulgarian authorities to forecast that the real annual growth rate of receivables from the non-government sector will drop below 25 per cent by the end of 2004.

Despite all these factors, by the end of 2004, banks will not decrease their interest in lending to small and medium-sized businesses, retail banking and development and offering new products and services. Although at a slower pace, the lending expansion to the non-financial sector is expected to continue. A major factor for the continuous interest of banks in lending remains the quest for new opportunities in the context of the potential or already existing saturation of the retail and corporate banking market and the continuing low rates of return on interest-bearing foreign assets.

In more general terms, medium-term bank strategies will reflect two groups of factors. First, this is the growing competition both within the banking sector itself and by non-banking financial institutions attacking market segments of both bank assets and bank liabilities. Second, commercial banks may be forced to comply with new regulations imposed by the BNB in relation to the new Basel standards for capital adequacy.

The year has been one of the most successful for the Bulgarian **capital market** so far. On an annual basis, market capitalization grew by 98 per cent, the stock exchange index SOFIX by 148

per cent, the trade volumes by 121 per cent, and the turnover by 90 per cent. The number of transactions exceeded that of 2002 by 176 per cent.

The COBOS (client order-book online system) system for electronic submission of orders via Internet by clients of the stock-exchange members was officially launched in the beginning of the year. The purpose of the implementation of this system was to facilitate Bulgarian broker dealers and to facilitate the filing of orders for sale or purchase of securities by individual and institutional investors from the country and from abroad (through a direct access to the trade system on the stock exchange). The launching of COBOS was a major step towards popularization, facilitation of access and, eventually, raising the liquidity of stock exchange trade.

A new, unified supervisory body, the Financial Supervision Commission, was established in 2003. The Investment Activity Supervision Division of the new Commission actually inherited the functions and structure of the former State Securities Commission. Reduction of costs, limiting the existing administration and raising efficiency were among the main motives underpinning the idea for consolidation of supervision.

The Act on Special Investment Purpose Companies was adopted during the year. The establishment of a greater variety of investment alternatives, the introduction for the first time of a special legal regulation of securitization of assets and the promotion of collective investment schemes are among the effects expected from the implementation of this law. The relevant ordinances also underwent serious developments in 2003. The FSC adopted the following entirely new ordinances: Ordinance on the Activity of Broker Dealers, Ordinance on the Prospectuses for Public Offering of Securities and Information Disclosure by Public Companies and Other Issuers of Securities, Ordinance on the Capital Adequacy and Liquidity of Broker Dealers, Ordinance on Permits for Performing Activity as a Stock Exchange, Organizer of an Unofficial Security Market, Broker Dealer, Investment Company, Managing Company and Special Investment Purpose Company, Ordinance on the Central Depository of Securities, and Ordinance on Tender Offering of Purchase and Exchange of Shares.

Amendments to the Rules of the Bulgarian Stock Exchange – Sofia AD and the Central Depository were adopted. According to these amendments, a minimum threshold of BGN 5,000 was introduced. All transactions exceeding that threshold must be settled by bank wires. In relation to the launching of the gross real time settlement system RINGS by the BNB, netting of cash payments between members was introduced and the term for settlement was reduced to two days.

The year will be remembered as the first full year of trade in compensatory instruments on the stock exchange. The concentration of trade on the Bulgarian Stock Exchange

– Sofia AD resulted in a higher level of transparency, clarity in pricing and increased liquidity. The disclosures about the so-called “problem lots” (which have been used in privatization transactions although their legitimate issuance is subject to court disputes) caused some uncertainty during the year. A number of changes were made to the Act on Transactions in Compensatory Instruments in order to solve this problem. On an annual basis, the compensatory instruments market marked a substantial growth, 48 per cent in volume, 92 per cent in turnover, and 216 per cent in number of transactions. This statistics is exclusive of transactions en bloc and inclusive of data about trade in investment vouchers. Vouchers were first registered for trade on the stock exchange in November. A total of 134 132 876 investment vouchers with par value of BGN 1 were registered.

One of the significant legislative changes was the new opportunity for the stock exchange to carry out technically (after commissioning by the Privatization Agency by force of a contract) centralized public tenders for sale of shares owned by the state or by the municipalities, as well as public tenders for sale of shares in limited liability companies owned by the state and the municipalities. This new possibility concerns mainly the privatization of non-public companies but nevertheless it could indirectly generate interest in the markets of the Bulgarian Stock Exchange – Sofia AD.

2003 was the most successful year by now in terms of the privatization via the stock exchange, as well. Growth but also the potential of the stock exchange mechanism for efficient privatization transactions was proved by the annual data. In 2003 (2002, respectively), 155 (61) transactions, with a turnover of BGN 16 490 690 (2 886 742) were conducted on the privatization market with Bulgarian levs. In 2003 (2002, respectively), 2 108 (33) transactions with a turnover of BGN 284 063 012 (309 013) were conducted on the privatization market with compensatory instruments (and investment vouchers in 2003). The stock exchange privatization of Bulgartabac Holding, DZI, Oil and Gas Exploration and Extraction AD, and Golden Sands, were among the key events during the year.

Despite the positive development, however, the capital market in Bulgaria remained rather unpopular as a channel of financial intermediation. At the end of 2003, the total market capitalization of the stock exchange was 7.89 per cent of the updated estimate of the GDP for 2003. Liquidity is increasing but generally remains at a low level. Market incentives are not sufficient to establish good corporate governance practices even in part of the public companies. A positive sign of improved culture and a signal of better efficiency of the market is the fact that the price dynamics of shares, especially at liquid positions, is increasingly influencing corporate events and fundamental factors (financial statement information and news about traded companies in particular).

It is expected that in 2004 trade on the stock exchange will remain active but without any substantial increase of liquidity. A factor supporting liquidity may be the new market players - special investment purpose companies, as well as newly licensed open-ended investment companies. The stock exchange index is expected to break its abrupt rise but it may well mark a growth on an annual basis, as well. An essential incentive generating interest in the market and its prospective development could be a continuation of the stock exchange privatization (especially if a minority share of the Bulgarian Telecommunication Company is offered, as expected). A further strengthening of supervision should be expected by the Financial Supervision Commission mainly with respect to information disclosure by issuers, market manipulations and insider trading. Despite the start of a futures market announced by the Bulgarian Stock Exchange – Sofia AD to be a priority for 2004, the implementation in practice is unlikely and during the year the systems for trade, striking and settlement of transactions in securities will not undergo any substantial changes.

2003 was marked by reforms in the **energy sector**. One of the most important events that will contribute for improving the business climate in the sector was the adoption of the Energy Act. It laid the foundations for the future building of a competitive environment in the sector. Competitive environment is necessary both for the further successful development of energy and for the general development of the Bulgarian economy. The considerable decrease of restriction regimes regulated by the Energy Act contributed for eliminating the entry barriers to the sector. It is in itself a prerequisite for the demonopolization of the Bulgarian energy sector and for saving time and costs for building new facilities for both new entrants and established energy producers. The right to access to the network by third parties is the new market model that will serve as a catalyst for the competitive behavior of the companies in the sector. Separating the purely commercial activities in electricity and gas sectors from the physical transfer and distribution will contribute to the establishment and entry of purely commercial companies in the electricity sector. In practice, this means a deeper specialization of the companies in the different types of activities and a higher quality of the services offered. The timely adoption of the underpinning regulations that will specify the exact frameworks of the prescriptions given by the law is of vital importance for the future efficient and effective implementation of the Energy Act. They should be adopted within six months after the act takes effect. Having in mind the delayed adoption of the regulations under the Energy and Energy Efficiency Act, it may be presumed that the end of 2004 is a more realistic deadline for their adoption. 2003 paved the way for the practical liberalization in the energy sector. The eligible consumer status given to ten enterprises by the State Energy Regulatory Commission allowed having 15 per cent of the consumer electricity in the country negotiated in accordance with market principles. The start of the privatization of electricity distribution companies was another major event in the sector. The

advance completion of the process of privatization of electricity distribution companies was impeded by the absence of stable legal regulation in the sector that would guarantee security to potential investors. The delay was also caused by the difference of opinions between the Privatization Agency and the Ministry of Energy and Energy Resources on certain issues related to the tender procedures for selling the electricity distribution companies. This case brought to the surface again the issue of the wrongly divided and intermingled competencies of the different government institutions with respect to the privatization processes. Despite the obstacles, the start of privatization was given in October and it is expected to end successfully by the end of 2004. As regards investments in the sector, it may be stated that 2003 was a good year having in mind the signed project for rehabilitation of Maritsa Iztok 3 Thermal Power Plant and the signed contract for rehabilitation of Maritsa Iztok 2 Thermal Power Plant by the Japanese company Mitsui&Co Ltd. The following year is expected to witness the implementation of the project for the construction of a new generation facility at the Maritsa Iztok 1 Thermal Power Plant that was long postponed due to the financial problems of the American company AES.

The trends in the regional development of the energy sector were also positive. The country's participation in the regional energy market will have considerable significance for the internationalization of the energy sector<sup>28</sup>. The liberalized import and export of electricity will result in more benefits for the consumers and will allow the country to generate additional revenue from trans-border transportation of electricity. The situation of national electricity producers will be a little more complicated as they will have to deal with external competition. What did not happen during the year in the sector was the identification of the investors that would start building the gas distribution network in the country. This delays the rate of penetration of natural gas as a cheaper alternative energy source for certain industrial enterprises and for the households.

In 2003, the prices of oil at the international markets were unstable. The most serious fluctuation was observed in March when quotations went down by USD 7. Their dynamics was mostly determined by OPEC's policy, by the demand and the reserves in the USA, and by the situation in the Middle East. Prices of oil and oil products in Bulgaria followed international market trends. They kept decreasing till April and then a smooth upward trend was established until in the last quarter they reached the levels from the beginning of the year. Excise duty tariffs were increased at the end of the year. This will probably result in a decrease of profits of fuel distributors on one hand, and increase of end consumer prices, on the other hand. An increase of prices of other consumer goods is also possible due to the eventual increase of the costs of transportation companies. Fuel demand price elasticity will determine the

<sup>28</sup> In 2003, Bulgaria signed a Memorandum for Establishment of a Regional Energy Market in Southeast Europe. A binding document is expected to get signed in 2004.

level of distribution of the heavier tax burden resulting from the excise duty increase.

The price at which Bulgargas sells natural gas in the domestic market is influenced by the prices of alternative fuels and by the prices of the dollar with a certain time lag. The lowest gas prices were registered in the third quarter of the year. This did not result in substantial positive effects since in this period the fertilizer industry and heating companies, which are among the largest consumers and their natural gas costs account for the highest share of their total costs, utilize a minimum portion of their production capacity. The high prices of gas during most of the year were the reason for the increase of the costs of manufacturers who use gas as their basic raw material. The final result is a reduction of their competitiveness and generally lower competitiveness of the country as a whole. A positive effect may be expected as a result of the substantially lower prices of natural gas coming into effect in the beginning of 2004.

In 2003, there was no substantial, visible progress of reforms in the **transport sector**. The legislative framework was moving at a low pace. By the end of the year, the draft laws that were expected to create favorable conditions for attracting private investment and for competition in the sector were not adopted. The large investment projects for the transport infrastructure did not witness any positive development during the year. The closing of Chapter 9: Transport Policy of the negotiations for EU membership may be considered as a positive event.

Draft Amendments to the Road Act were developed with a view to advance automobile transport and to harmonize Bulgarian legislation with EU requirements. The draft law was adopted in the beginning of 2004. It contains the principles of attracting larger investments for building new road facilities and certain road sectors through public-private partnership. Concession contracts were chosen as the most appropriate form of relieving the government from the obligation to build new road infrastructure. A new, more efficient scheme for transfer of financial resources is planned for the maintenance of existing infrastructure. There was no serious progress under the Recovery of Transit Roads III Project, although the deadline for project completion was the end of 2003, as indicated in the financial memorandum between the EC and Bulgaria.

Railway transport did not witness any serious changes in the past year. Private railway sector operators were not introduced. This is probably one of the main reasons that the processes and efforts to introduce and implement more flexible market methods for management of the state-owned companies in the sub-sector were not enhanced. The implementation of railway transport projects under the ISPA program is lagging behind. The monopoly of the Bulgarian State Railways, as well as the general economic growth, allowed the company to increase the volume of cargo by 8.6 per cent compared to the previous year.

The delayed concession on Varna and Bourgas airports is largely a result of the slow pace of developing the legislation regulating the issues in the sub-sector. The draft Amendments to the Civil Aviation Act are still under discussion in the National Assembly. A future delay of these processes may have a negative effect on the renovation of, as well as on the capacity and quality of service offered at the airports on the Black Sea. This will have an indirect effect on the future inflow of tourists willing to visit the Bulgarian Black Sea resorts. Bulgaria Air remained state-owned and retained its monopoly with respect to the destinations it services under bilateral agreements. Holding the exclusive carrier right is the company's most significant advantage in its prospective privatization. This advantage remains due to Bulgaria's denial to join the *Single European Sky* Agreement. Bulgaria's non-participation in this agreement ensures the dominating position of the Bulgarian airline companies. On the other hand, it deprives consumers of improved quality generated by the competition in the sector and of the opportunity to use the services of low-cost companies. The implementation of the Reconstruction, Development, and Expansion of Sofia Airport Project is delayed. Eventually, the deadlines for project implementation were extended and gross costs thereon increased.

As regards water transport, a will for changes was demonstrated and specifically expressed in the Strategy for Development of River and Sea Transport and Ports. Certain specification and updating is expected for a large number of the measures and directions given in the strategy with a view to make it a feasible and efficient document. A step forward in the sub-sector in 2003 was the privatization of Varna Dockyard. The procedures for the overall completion of the transaction were quite extensive but it should be noted that the privatization of the dockyard is a good prerequisite for its future development.

The major events which the **high technology and communications sector** was looking forward to in 2003 and which were expected to have a substantial influence on the future development of the industry, were the adoption of a new Telecommunications Act and the privatization of the Bulgarian Telecommunications Company. The achievement of these two goals is closely related to the overall future development of the sector and the creation of real competitive market environment, which would be to the benefit for all business and individual consumers.

Despite the excessive delay and the difficulties, at the end of the year Bulgaria had an entirely new Telecommunications Act guaranteeing both the liberalization of the telecommunication market and the rights of the consumers in the new sector environment. This Bulgarian law does not reflect the latest EU directives (adopted in 2003), but it follows the prescriptions of the previous series of directives that in essence refer to the initial state after liberalization of telecommunications. This state reflects precisely our level of development of the market.



In 2003, for various reasons, the Government did not succeed in making the privatization of the BTC although at the end of the year the signing of the documents with Advent International was decided as final. Placing a portion of the shares in BTC shares on the stock exchange after the privatization was expected eagerly throughout the year but it did not take place in 2003. The great interest on behalf of the stock exchange is determined by the fact that, according to the Government's commitments, compensatory instruments would be allowed for purchasing BTC shares.

The first sale of shares in a technology company on the stock exchange is eloquent of the maturity of the information and communication technology sector. Based on the interest aroused by the trade, it may be concluded that currently, Bulgaria has a potential to implement such transactions but most companies obviously fail to accept the appearance on the stock exchange as a serious source of raising financial capital. This fact has mainly a negative effect since the existence of sufficiently developed companies in the sector in combination with a capital market "hungry" for high quality issues may result in a win-win situation for both sides.

The year 2003 proved extremely favorable for the development and expansion of the Internet market and related services (VoIP, e-commerce, Internet advertising, etc.) A decrease of web-access prices was observed over the entire year together with an expansion of access opportunities – through cable TV networks or local area networks (LAN). At the same time, the absolute number of Internet users in Bulgaria has not increased (according to different surveys, Internet users are approximately 10 – 14 per cent of the population). Obviously, market development is mainly expressed in providing better services at lower prices to the existing users in the country.

Serious developments were observed in the communications sub-sector where the Communications Regulation Commission (CRC) licensed five new companies for providing voice services through fixed telephone networks. Together with that, the distribution of alternative communication services (VoIP) among business and individual users has marked a serious growth in 2003. Although there are no official data, it would be realistic to consider that VoIP use has increased more than twice during the year.

The E-Government Strategy adopted in 2002 envisioned rapid development of conditions for providing e-Government services. Unfortunately, 2003 will not be remembered with many real results in this area. The so-called pilot project promoted largely in September earned the disapproval of the professionals in the area. Moreover, its implementation was not in line with basic issues in the Strategy and generated further criticism by the experts. Through the end of the year, the e-services offered by the government are just a few, and the price for obtaining an

electronic signature (from two licensed providers) was too high to contribute for the more intensive use of such services.

The Strategic Plan for Development of Bulgaria's IT industry is of significant importance for the future development of the information and communication technologies. The Plan was developed jointly by the major sector-related industrial organizations (BAIT, BIBA, and BASSCOM) with the support of the United States Agency for International Development (USAID). The final version of the document was presented to the government and was favorably accepted. The mere fact that in this case the initiative comes from the private sector and the largest industrial organizations in the field stand behind the document is rather positive. This means that the information and telecommunication companies in Bulgaria have realized the advantages of uniting their efforts for a common cause and have managed to overcome certain differences that, only until several years ago, stood in the way of the sector's development. We can only hope that soon there will be some practical implementation of the commitments and recommendations in the strategic plan. Such an event will definitely have a positive effect on the local information and telecommunication technology sector.

In 2003, **tourism** was one of the most successful economic sectors. The data about the revenues from tourism are quite significant. According to information from BNB, in 2003 revenues from tourism reached USD 1.622 b, registering an increase of 21.6 per cent compared to 2002 when they amounted to USD 1.334 b. Bulgarians' spending on tourism abroad amounted to USD 735.8 m, registering an increase of 19.4 per cent compared to the previous year (USD 615.7 m). In 2003 net revenues from tourism amounted to USD 886.8 m, registering an increase of 23 per cent compared to 2002.

In the past year, total number of foreign tourists reached 4.4 m people, registering an increase of 18 per cent. EU Member States, i.e. Greece, Germany, and Great Britain, accounted for the highest number of tourists. A positive trend emerged in 2003 both in terms of seaside tourism and mountain tourism. Bulgaria is gradually regaining its positions on the markets of Central and Eastern European countries, including Russia, Hungary, Czech Republic, Slovak Republic, and Poland.

According to the World Tourism Organization, Bulgaria takes one of the first places in Europe in terms of tourist industry growth dynamics, along with the other most attractive tourist destinations on the Old Continent such as Croatia and Portugal.

The prerequisites for good achievements in tourism are connected with several circumstances. First, private sector investments in specialized infrastructure and in substantial improvement of the services offered to foreign tourists. Second, Bulgaria was not seriously affected by two major factors, which

had effect on global tourism development – the war in Iraq and the cases of SARS, which resulted in overall drop of travels throughout the world.

In 2003, there were a number of new investments in expanding and innovating facilities. New hotels, sports and animation facilities, etc. were built. Such investments were made both in seaside and in winter resorts. Investment activity is expanding along the southern Black Sea coast. Winter resorts are also developing well. The largest investment in a Bulgarian winter resort was that in the cable car in Bansko amounting to USD 30 m. Efforts are made to prolong the active season in seaside and mountain resorts. Seaside and skiing tourism are successfully combined with congress, spa, rehabilitation, cultural and eco tourism.

A number of new ideas for structural and organizational changes in the sector were launched to respond to the requirements of modern tourist industry. This presupposes the development of new strategies in the field area by both the Government and the companies. A Concept for Development of a New Model for Management of Resorts of National Importance was proposed for discussion. This discussion has not finished yet.

The amendments to the Tourism Act were passed on first reading. The most important amendment is the set up of an Agency for Tourism (AT) within the Ministry of Economy. The Agency for National Tourist Advertising and Information will be part of the AT. Two expert committees will be established under the AT; one for registration of tour operators and one for categorization of sites.

Certain ordinances were also amended, i.e. the Ordinance on the Licensing of Tour Operator and Tourist Activity. The requirements for minimum staff number of tour operators were repealed. The Ordinance on Categorization of Tourist Sites was also amended and now the high requirements to high category hotels will only apply to sites designed after July 1, 2003.

Some of the problems in Bulgarian tourism, which have been pointed out and discussed many times, persisted. These include the low quality of transport infrastructure, insufficient staff qualification, absence of professional management, poor hygiene and attitude to the clients. Tourism is already suffering from a lack of qualified staff. Changes in the educational system are mainly required to solve this problem, i.e. updating the curricula in the area of tourism, practical courses and internships in tourist sites in the country. Another possible solution is the active participation of the tourist business in the training process.

National advertising and marketing did not witness any substantial changes. The funds allocated for this purpose are always insufficient. The building of an integrated national tourist information base is delayed, while the existence of such

a database would considerably improve the popularization of the country around the world.

The legislation in the area of **agriculture** is being harmonized with the *acquis communautaire* at accelerated pace. The mechanisms of providing support to farmers, the development of a database on the condition of the sector as a major instrument to defend Bulgaria's position in the accession negotiations with the EU and the elaboration of development strategies for key branches, register permanent improvement. The census of operating farms was completed. That will help defend to the maximum extent Bulgaria's position in the negotiations with the EU on the financial framework and quotas. A number of projects for land consolidation were launched as a serious manifestation of the intentions of the Ministry of Agriculture and Forestry and of donors to solve this problem of vital importance for the successful restructuring of the Bulgarian agriculture. There was a slight revival on the land market, characterized by a negligible decrease in the number of sales and purchases, a slight increase of the average price and an improvement of rental relations. Supply remains higher than demand and overall, the price of agricultural land remains comparatively low.

The poor grain crop in Bulgaria, as well as worldwide, generated concerns about shortage of grain to feed the people and the live stock on the one hand, and about a serious rise of prices as a result of the higher prices on the international commodity markets, on the other hand. The grain crisis, conditioned by the poor crop and the aggravated situation on the international market, as well as by national market deformations, the existing shadow economy, the ambiguous and largely unregulated market relations, absence of a real intervention agency whose actions would be based on a clear long-term policy and justified measures formulated in advance, caused ardent debate and contradictory assessments of the need and efficiency of state intervention on the market. Nevertheless, the intervention calmed down the market and stabilized the price at a level corresponding to the specific conditions on the international market. This measure generated protests by the market participants, as preconditions for unfair competition were created and the market relationship was disturbed. The ambiguous intervention policy of the government, which was oriented towards solving problems "piece by piece" and imposing political/social reasons on the business, as well as the absence of long-term crisis management measures make the market unpredictable and impede normal market relations. This situation outlines the need to quickly establish and make operational an intervention agency similar to the one in place in the EU.

The operation of the Agriculture Fund and the expanded financing opportunities under the SAPARD program are positive factors from the perspective of the needs of agricultural producers. The Agriculture Fund confirms its positions of a financing and intervention agency by expanding its activity and

developing its administrative capacity. In 2003, BGN 210 m was provided, of which BGN 40 m was envisaged for direct support of producers. A total of BGN 70 m was allocated for investment programs of the Fund, i.e. Plant Growing, Live Stock Breeding, and Agricultural Equipment. By decision of the Managing Board, loans for purchase of new equipment with the financial support of the Fund may be taken at preferential interest rates from commercial banks with which the Fund has signed refinancing contracts. Thereby the volume of purchased equipment increased, as well as the number of projects refinanced by commercial banks, and a higher number of farmers participate in the program. Farmers received additional financing for growing different crops in accordance with the different Fund lines. In this case, the principle applied was that of stage-by-stage introduction of European assistance mechanisms through direct payments instead of loans.

The efforts to clarify and expand farmers' capacity to obtain funding from SAPARD continue. Just in a year, over 600 projects with a total value of BGN 470 m were approved under the first three measures. Following the decision of the European Commission of August 23, 2003<sup>29</sup>, Bulgaria was entitled to manage the funds under seven new SAPARD measures. Projects for establishing organizations of producers, building markets, forestry, forestation of agricultural lands, investment in forests, processing and marketing of forest products are eligible to applying for these measures. Two of the new measures are entirely geared towards the public sector and the municipalities will be their beneficiaries. Basically, this is the possibility to apply with projects for renovation and development of villages, conservation of cultural heritage and traditions, and development and improvement of country infrastructure. One of the new accredited measures provides the opportunity to granting funds to training institutions for training courses targeting farmers and tobacco producers, owners and users of forests and all other individuals involved in agriculture. The funds from the technical assistance measure will be used for information campaigns geared towards potential applicants for funding under the program.

Despite the constant improvement of the conditions for access to the Program and the increase of the number of approved projects, the general observation of the EU Monitoring Committee is that Bulgaria was the first to start program implementation, but it is now lagging far behind the other candidate countries in the utilization of SAPARD funds for the financing of national agriculture. The main reason for that lies in the difficulties farmers face in the preparation of reliable projects, the relatively hard application conditions and the incapacity to provide funding of their own.

On May 8, 2003, the American Senate ratified the pre-accession protocol for **Bulgaria's membership in NATO**. During the Italian

presidency, in the second half of the year Bulgaria managed to close three **EU negotiation** chapters. These were Chapter 9, *Transport*, Chapter 22, *Environment*, and Chapter 24, *Justice and Home Affairs*. The total number of negotiation chapters closed through December 31, 2003, is 26. The European Commission's Regular Report on Bulgaria's progress was published in November. The country's macroeconomic stability was given a good grade. The recommendations to Bulgaria included in the Regular Report concern the flexibility of markets and the need of further structural reforms, including reforms in the administration and the judiciary system. On December 12 – 13, 2003, in Brussels, the European Union made a decision for Bulgaria and Romania to join the EU in January 2007 if they are ready for full membership.

In 2003, the efforts to implement a successful **regional policy** continued in order to achieve a balanced and sustainable development of the Bulgarian regions, to reduce disproportions between the different regions and to achieve gradual social and economic cohesion with the EU.

An important moment in this area was the adoption on first reading of the new Regional Development Act. This law is an appropriate legal framework for ensuring full compatibility with the EU policies and regulations including operations financed from the pre-accession funds. The new law, unlike the old one, contains a detailed description of the planning regions and the target impact regions, the regional development planning and programming activities, the management structure. The new law allows implementing a government policy backed by the relevant planning and funding in combination with efficient local government at regional level.

In 2003, local governance strengthened further its position of an irreversible process with the respective achievements and problems. Major achievements in the field include: changing legislation which is under harmonization with the *acquis*, local-central government dialogue, accumulated expertise, common activities of the municipalities within a common association, building public-private partnership at local level, promoting the established network of partner organizations and programs, more active involvement of the Bulgarian municipalities in the EU integration process, partnership with international organizations in studying and implementing the best practices.

In the area of legislation, substantial efforts were made to distinguish the powers and cooperation of local and central authorities with a view to clearly define the rights and responsibilities of the local governance authorities within their sphere of competence and achieve financial and property independence of the municipalities through increased tax powers and greater independence in the draw up and management of municipal budgets. A specific step towards such independence is the implementation of the decision that allows municipalities

<sup>29</sup> Commission Decision 2003/614/EC, Official Journal L 213, 23.8.2003, p. 10-11.

to collect local taxes and fees. There are concerns, however, that a number of municipalities are not ready to do that.

New information and service centers for the public were set up in the Bulgarian municipalities. New business centers and business incubators were also created and a number of other forms of providing information and advice to the public and to the business were introduced.

The main problems facing efficient local governance are associated again with the insufficient awareness of the need of an active dialogue between the local and central government which would enhance the decentralization processes.

The local elections for mayors and municipal councilors held at the end of October 2003 were the most important event that had an unquestionable effect on regional development. At a number of forums, the new local government representatives expressed their willingness to follow the continuity in terms of the policy for social and economic development of municipalities, the continuity in the administration and the municipal council, as well as the continuity in the established contacts and their further development. The new local governance authorities will lead the Bulgarian municipalities in the EU upon the accession in 2007. This fact predetermines one of the major priorities in their activity, i.e. to prepare the municipalities for full EU membership. In the beginning of their term of office, they outlined the problems in this regard at a number of meetings and forums. Some of these problems are the lack of sufficient information and knowledge of the EU structures and decision-making mechanisms, the fact that the tasks related to the forthcoming EU accession are not clear, the lack of sufficient financial, human and administrative resources, the inefficient cooperation with the central level.

Solving these problems would require long-term specialized training in development of projects for funding from the EU funds, information campaigns and discussion forums at the local level on preparation and EU accession issues, building expert capacity for working with EU programs on municipal level, improved access to information about the opportunities to apply for EU programs. In this regard, it is necessary to improve and enhance the partnership between non-government organizations, the central government and the municipal bodies and the presentation of successful municipal practices for utilization of EU funds.



# ANNEX 1: MAIN INDICATORS FOR THE FOURTH QUARTER OF 2003

Industry	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
<b>Economic dynamics</b>																	
<b>Industrial production, volume index, previous month =100, %</b>																	
2003	86.5	96.7	116.7	91.8	94.6	111.8	103.1	93.7	109	102.2	99.5	107.7					
2002	81.5	99.7	109.2	101.6	96.5	106.3	105.2	95.8	103.9	100.4	105.3	101.6	-	-	-	-	-
<b>Industrial production, volume index, corresponding month of the previous year = 100, %</b>																	
2003	115.4	115.4	123.4	111.9	109.6	115.4	113	110.3	115.9	117.9	111.3	118.2					
2002	96.6	94.2	96	111.5	104.5	107.6	112	104.6	109.7	105.6	109.9	104	-	-	-	-	-
<b>Industrial production, from the beginning of the year, volume index, corresponding period of the previous year = 100, %</b>																	
2003	115.4	115.4	118.2	116.4	115	115.4	115	114.4	114.5	114.8	114.5	114.8					
2002	96.6	95.4	95.6	99.3	100.3	101.5	103	103.2	104	104.1	104.7	104.6	-	-	-	-	-
<b>Industrial sales, total, volume index, previous month =100, %</b>																	
2003	86.2	96.8	119.6	92.6	98.5	108.8	102.5	93.9	106.3	103.4	98.2	107.3					
2002	82.3	97.9	106.8	108.4	93	108.4	107	95.5	101.9	99	104.3	104.7	-	-	-	-	-
<b>Industrial sales, total, corresponding month of the previous year = 100, %</b>																	
2003	117.7	116.4	130.4	111.3	117.8	118.3	113.4	111.4	116.3	121.5	114.4	117.3					
2002	90.7	89.7	90.5	108.9	96.3	104	110	105.1	108.9	100.3	105.8	105.6	-	-	-	-	-
<b>Industrial sales, total, from the beginning of the year, volume index, corresponding period of the previous year = 100, %</b>																	
2003	117.8	117.1	121.6	118.8	118.6	118.6	117.7	116.9	116.8	117.3	117	117					
2002	90.7	90.2	90.3	94.7	95	96.5	98.5	99.3	100.4	100.4	100.9	101.3	-	-	-	-	-
<b>Domestic trade</b>																	
<b>Trade and repairing activities, total, net receipts from sales, volume index, previous month =100, %</b>																	
2003	71.0	102.7	107.1	101.7	102.6	102.9	106.5	98.2	104.2	102.7	96.8	114.4					
2002	-	113.3	111.7	98.9	98.2	101.6	111.6	102.4	101.4	108.3	96.6	109.5	-	-	-	-	-
<b>Trade of motor vehicles and motorcycles, repair of motor; retail trade of automotive fuel, net receipts from sales, volume index, previous month =100, %</b>																	
2003	76.7	98.0	107.3	102.7	103.4	107.0	105.9	100.1	102.8	105.2	99.2	108.1					
2002	-	99.7	116.9	95.4	99.6	107.7	106.7	97.0	102.7	107.9	101.6	102.4	-	-	-	-	-
<b>Wholesale and commission trade, net receipts from sales, volume index, previous month =100, %</b>																	
2003	70.2	104.1	106.7	101.2	102.2	102.2	107.1	97.3	104.8	102.3	96.4	114.7					
2002	-	118.3	112.0	99.1	97.3	100.5	113.7	103.0	100.9	109.3	95.4	109.9	-	-	-	-	-
<b>Retail trade, repair of personal and household goods, net receipts from sales, volume index, previous month =100, %</b>																	
2003	71.0	98.9	109.4	104.1	104.3	103.4	103.7	101.1	102.5	103.0	96.9	117.4					
2002	-	100.8	106.4	100.1	101.7	102.6	105.1	103.3	102.9	103.7	99.6	112.6	-	-	-	-	-
<b>Trade and repairing activities, total, net receipts from sales, volume index, corresponding month of the previous year = 100, %</b>																	
2003	106.1	107.2	108.1	110.0	110.1	108.0	107.2	104.6	105.7	104.9	102.4	105.8					
2002	93.1	100.1	97.9	103.0	100.1	101.9	106.6	108.9	110.6	109.5	109.0	111.1	-	-	-	-	-

# ANNEX 1: MAIN INDICATORS FOR THE FOURTH QUARTER OF 2003

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
	Trade of motor vehicles and motorcycles, repair of motor; retail trade of automotive fuel, net receipts from sales, volume index, corresponding month of the previous year = 100%																
2003	103.5	98.8	100.6	101.2	102.5	104.1	103.8	102.3	103.1	103.9	101.5	105.2	-	-	-	-	-
2002	97.3	106.7	103.1	103.1	98.4	98.5	98.7	98.9	101.4	102.9	105.3	104.7	-	-	-	-	-
	Wholesale and commission trade, net receipts from sales, volume index, corresponding month of the previous year = 100, %																
2003	107.5	109.5	109.8	112.0	112.2	109.0	107.7	104.6	105.8	104.5	101.7	105.5	-	-	-	-	-
2002	90.9	98.7	96.4	103.2	100.3	102.6	108.3	110.9	113.5	111.6	110.8	113.4	-	-	-	-	-
	Retail trade, repair of personal and household goods, net receipts from sales, volume index, corresponding month of the previous year = 100, %																
2003	102.0	102.1	104.4	106.4	105.5	105.9	106.9	106.2	106.9	108.1	106.3	108.0	-	-	-	-	-
2002	101.0	103.4	101.6	101.9	100.2	101.1	104.5	106.2	104.1	103.7	103.3	104.9	-	-	-	-	-
	Trade and repairing activities, total, net receipts from sales, volume index, from the beginning of the year, corresponding period of the previous year =100, %																
2003	106.1	107.8	108.0	108.7	109.0	108.8	108.5	108.0	107.7	107.4	106.9	106.7	-	-	-	-	-
2002	93.1	96.7	95.4	97.3	97.9	98.5	99.8	101.0	102.1	102.9	103.5	104.3	-	-	-	-	-
	Trade of motor vehicles and motorcycles, repair of motor; retail trade of automotive fuel, net receipts from sales, volume index, from the beginning of the year, corresponding period of the previous year =100, %																
2003	103.5	101.5	101.2	101.3	101.6	102.1	102.3	102.3	102.4	102.6	102.5	102.8	-	-	-	-	-
2002	97.3	101.8	102.3	102.5	101.6	101.0	100.7	100.4	100.5	100.8	101.3	101.7	-	-	-	-	-
	Wholesale and commission trade, net receipts from sales, volume index, from the beginning of the year, corresponding period of the previous year =100, %																
2003	107.5	109.7	110.0	110.7	111.0	110.7	110.2	109.4	108.9	108.4	107.7	107.5	-	-	-	-	-
2002	90.9	94.9	93.2	95.7	96.6	97.6	99.2	100.7	102.2	103.2	104.0	104.9	-	-	-	-	-
	Retail trade, repair of personal and household goods, net receipts from sales, volume index, from the beginning of the year, corresponding period of the previous year =100, %																
2003	102.0	102.6	103.3	104.0	104.3	104.6	105.0	105.2	105.4	105.7	105.7	106.0	-	-	-	-	-
2002	101.0	102.3	102.1	102.1	101.7	101.6	102.0	102.6	102.8	102.9	102.9	103.2	-	-	-	-	-
Inflation																	
	Inflation (Consumer price index - 100), previous month =100, %																
2003	0.6	0.1	0.4	0.3	-0.6	-2.2	0.9	0.8	0.9	0.7	1.8	1.8	-	-	-	-	-
2002	2.7	1.6	0.8	-0.1	-2.1	-1.7	0.1	-0.7	0.8	1	0.2	1.2	-	-	-	-	-
	Inflation (Consumer price index - 100), December of the previous year = 100, %																
2003	0.6	0.8	1.2	1.5	0.8	-1.4	-0.5	0.3	1.2	1.9	3.8	5.6	-	-	-	-	-
2002	2.7	4.4	5.2	5.1	2.9	1.1	1.2	0.6	1.4	2.4	2.5	3.8	-	-	-	-	-
	Inflation (Consumer price index - 100), corresponding period of the previous year = 100, %																
2003	1.7	0.2	-0.2	0.2	1.7	1.2	2.0	3.5	3.6	3.3	5.1	5.6	0.6	1.1	3.1	4.7	2.3
2002	7.0	8.4	9.2	9.2	6.9	5.2	5.5	4.5	4.0	3.2	3.2	3.8	8.2	7.1	4.6	3.4	5.8
Employment and unemployment																	
	Unemployed persons registered, total, end of the period, number																
2003	646 757	611 727	581 350	552 068	528 718	506 424	489 343	480 881	472 614	476 326	489 618	500 664	581 350	506 424	472 614	500 664	500 664
2002	687 805	683 894	668 972	678 637	673 803	659 032	653 329	650 018	644 718	644 298	624 946	602 524	668 972	659 032	644 718	602 524	602 524
	Unemployment (Employment Agency, ratio to the economically active population from the population census in 2001), end of the period, %																
2003	17.46	16.51	15.69	14.90	14.27	13.67	13.21	12.98	12.76	12.86	13.22	13.52	15.69	13.67	12.76	13.52	13.52
2002	18.57	18.46	18.06	18.32	18.19	17.79	17.64	17.55	17.4	17.39	16.87	16.27	18.06	17.79	17.40	16.27	16.27

# ANNEX 1: MAIN INDICATORS FOR THE FOURTH QUARTER OF 2003

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
<b>Newly opened vacant jobs, end of the period, number</b>																	
2003	1 759	2 024	2 136	2 480	2 349	6 076	3 890	2 782	2 804	3 365	3 516	3 999	2 136	6 076	2 804	3 999	3 999
2002	1 588	4 177	3 284	3 420	2 437	2 055	2 011	3 272	2 802	2 270	2 651	1 926	3 284	2 055	2 802	1 926	1 926
<b>Employed person, total, end of the period, number</b>																	
2003	1 946 834	1 991 623	2 016 828	2 043 764	2 054 972	2 068 694	2 075 881	2 067 291	2 063 429	2 050 282	2 034 033	2 005 369	2 016 828	2 068 694	2 063 429	2 005 369	2 005 369
2002	1 878 628	1 883 392	1 890 173	1 895 911	1 905 823	1 913 121	1 917 999	1 914 477	1 925 092	1 917 214	1 918 643	1 911 216	1 890 173	1 913 121	1 925 092	1 911 216	1 911 216
<b>Employed person, public sector, end of the period, number</b>																	
2003	730 873	757 271	765 688	771 192	771 746	775 281	778 647	776 774	778 293	772 629	768 505	758 795	765 688	775 281	778 293	758 795	758 795
2002	761 630	762 192	760 562	749 826	745 729	743 092	737 200	735 424	740 543	735 825	747 422	756 733	760 562	743 092	740 543	756 733	756 733
<b>Employed person, private sector, end of the period, number</b>																	
2003	1 215 961	1 234 352	1 251 140	1 272 572	1 283 226	1 293 413	1 297 234	1 290 517	1 285 136	1 277 653	1 265 528	1 246 574	1 251 140	1 293 413	1 285 136	1 246 574	1 246 574
2002	1 116 998	1 121 200	1 129 611	1 146 085	1 160 094	1 170 029	1 180 799	1 179 053	1 184 549	1 181 389	1 171 221	1 154 483	1 129 611	1 170 029	1 184 549	1 154 483	1 154 483
<b>Fiscal review</b>																	
<b>State budget</b>																	
<b>Revenues of the Consolidated State Budget, total, BGN million</b>																	
2003	1 029.2	1 944.8	3 220.6	4 631.2	5 813.3	6 830.5	8 054.1	9 158.9	10 311.4	11 573.2	12 657.0	14 072.0	3 220.6	6 830.5	10 311.4	14 072.0	14 072.0
2002	889.1	1 752.7	2 782.3	4 040.8	5 156.1	6 064.4	7 247.7	8 194.7	9 180.6	10 312.3	11 315.3	12 524.8	2 782.3	6 064.4	9 180.6	12 524.8	12 524.8
<b>Expenditures of the Consolidated State Budget, total, BGN million</b>																	
2003	1 130.6	2 105.4	3 109.8	4 221.5	5 195.0	6 203.4	7 402.7	8 429.7	9 463.7	10 602.5	11 758.1	14 071.1	3 109.8	6 203.4	9 463.7	14 071.1	14 071.1
2002	1 020.3	1 905.9	2 821.1	3 928.6	4 816.5	5 733.6	6 843.6	7 778.0	8 688.8	9 667.1	10 789.5	12 743.1	2 821.1	5 733.6	8 688.8	12 743.1	12 743.1
<b>Consolidated State Budget deficit (-) / surplus (+), BGN million</b>																	
2003	-101.5	-160.6	110.8	409.7	618.3	627.1	651.4	729.2	847.8	970.7	898.9	0.9	110.8	627.1	847.8	0.9	0.9
2002	-131.2	-153.2	-38.8	112.2	339.6	330.8	404.1	416.7	491.8	645.2	525.8	-218.3	-38.8	330.8	491.8	-218.3	-218.3
<b>Revenues of the Republican Budget, total, BGN million</b>																	
2003	651.3	908.4	1 937.0	2 878.1	3 626.4	4 221.2	4 985.2	5 637.7	6 279.0	7 051.8	7 684.9	8 441.6	1 937.0	4 221.2	6 279.0	8 441.6	8 441.6
2002	521.9	985.5	1 585.0	2 364.3	3 042.6	3 540.5	4 242.3	4 783.1	5 355.4	6 076.4	6 647.0	7 289.4	1 585.0	3 540.5	5 355.4	7 289.4	7 289.4
<b>Expenditures of the Republican Budget, total, BGN million</b>																	
2003	737.0	1 195.6	1 846.2	2 594.1	3 016.6	3 639.2	4 372.7	4 979.0	5 520.4	6 200.7	6 952.7	8 552.2	1 846.2	3 639.2	5 520.4	8 552.2	8 552.2
2002	367.7	869.5	1 376.1	2 113.1	2 531.4	3 018.5	3 718.5	4 205.2	4 697.0	5 252.8	5 949.2	7 286.0	1 376.1	3 018.5	4 697.0	7 286.0	7 286.0
<b>Republican Budget cash deficit (-) / surplus (+), BGN million</b>																	
2003	-85.7	-287.2	90.8	284.0	609.7	582.0	612.4	658.7	758.5	851.1	732.2	110.6	90.8	582.0	758.5	110.6	110.6
2002	154.2	116.0	208.9	251.3	511.1	521.9	523.8	577.9	658.4	823.5	697.8	3.4	208.9	521.9	658.4	3.4	3.4
<b>Government and government guaranteed debt</b>																	
<b>Government and government guaranteed debt, BGN million</b>																	
2003	17 548	17 639	17 560	17 680	17 062	17 365	17 467	17 858	17 195	17 140	16 931	16 510	17 560	17 365	17 195	16 510	16 510
2002	20 993	20 917	20 859	20 103	19 502	18 855	18 993	18 964	18 929	18 667	18 627	18 180	20 859	18 855	18 929	18 180	18 180
<b>Domestic government and government guaranteed debt, BGN million</b>																	
2003	2 114	2 207	2 291	2 246	2 226	2 234	2 215	2 237	2 218	2 194	2 248	2 241	2 291	2 234	2 218	2 241	2 241
2002	1 897	1 890	1 917	1 927	1 908	1 949	1 973	1 988	2 030	2 042	2 088	2 112	1 917	1 949	2 030	2 112	2 112

# ANNEX 1: MAIN INDICATORS FOR THE FOURTH QUARTER OF 2003

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
<b>Foreign government and government guaranteed debt, BGN million</b>																	
2003	15 434	15 431	15 270	15 434	14 836	15 131	15 251	15 622	14 977	14 947	14 683	14 269	15 270	15 131	14 977	14 269	14 269
2002	19 096	19 027	18 942	18 177	17 594	16 906	17 020	16 976	16 899	16 625	16 539	16 069	18 942	16 906	16 899	16 069	16 069
<b>Government and government guaranteed debt, ratio to the annual GDP, %</b>																	
2003	49.7	50.0	49.8	50.1	48.4	49.2	49.5	50.6	48.7	48.6	48.0	47.8	49.8	49.2	48.7	47.8	47.8
2002	68.2	68.0	67.6	65.3	63.4	61.3	61.8	61.6	61.5	60.6	60.5	56.0	67.6	61.3	61.5	56.0	56.0
<b>Domestic government and government guaranteed debt, ratio to the annual GDP, %</b>																	
2003	6.0	6.3	6.5	6.4	6.3	6.3	6.3	6.3	6.3	6.2	6.4	6.5	6.5	6.3	6.3	6.5	6.5
2002	6.2	6.1	6.2	6.3	6.2	6.3	6.4	6.5	6.6	6.6	6.8	6.5	6.2	6.3	6.6	6.5	6.5
<b>Foreign government and government guaranteed debt, ratio to the annual GDP, %</b>																	
2003	43.7	43.7	43.3	43.7	42.0	42.9	43.2	44.3	42.4	42.4	41.6	41.3	43.3	42.9	42.4	41.3	41.3
2002	62.0	61.8	61.4	59.0	57.2	55.0	55.4	55.2	54.9	54.0	53.7	49.5	61.4	55.0	54.9	49.5	49.5
<b>Domestic government debt, total, BGN million</b>																	
2003	2 112	2 206	2 289	2 245	2 225	2 234	2 216	2 237	2 218	2 194	2 248	2 241	2 289	2 234	2 218	2 241	2 241
2002	1 891	1 884	1 912	1 922	1 903	1 945	1 973	1 988	2 027	2 039	2 085	2 110	1 912	1 945	2 027	2 110	2 110
<b>Debt on Government Securities issued for budget deficit financing, BGN million</b>																	
2003	1 515	1 609	1 696	1 659	1 659	1 658	1 638	1 653	1 654	1 633	1 697	1 704	1 696	1 658	1 654	1 704	1 704
2002	1 144	1 139	1 172	1 198	1 201	1 269	1 286	1 307	1 351	1 369	1 418	1 462	1 172	1 269	1 351	1 462	1 462
<b>Debt on Government Securities issued for structural reform, BGN million</b>																	
2003	596	597	593	586	567	576	578	584	564	560	552	537	593	576	564	537	537
2002	746	745	740	724	702	677	684	677	676	670	667	648	740	677	676	648	648
<b>Domestic government guarantees, BGN million</b>																	
2003	1.8	1.5	1.2	0.9	0.5	0	0	0	0	0	0	0	1.2	0.0	0.0	0.0	0.0
2002	6.4	6	5.6	5.1	4.5	3.9	3.7	3.3	3	2.6	2.3	1.9	5.6	3.9	3.0	1.9	1.9
<b>Foreign government debt, USD million</b>																	
2003	8 109	8 092	8 090	8 356	8 536	8 415	8 372	8 284	8 461	8 417	8 530	8 719	8 090	8 415	8 461	8 719	8 719
2002	7 925	7 921	7 921	7 840	7 936	8 103	7 997	7 997	7 967	7 849	7 862	7 978	7 921	8 103	7 967	7 978	7 978
<b>Foreign government guaranteed debt, USD million</b>																	
2003	426	415	416	428	432	426	453	444	461	464	474	496	416	426	461	496	496
2002	508	496	503	505	509	529	524	538	541	536	533	546	503	529	541	546	546
<b>Foreign economic relations and foreign investments</b>																	
<b>Balance of Payments</b>																	
<b>Current account, million USD</b>																	
2003	-166.0	-155.6	-93.3	-388.2	-226.5	22.8	26.3	145.5	16.0	-210.4	-300.4	-318.1	-414.9	-591.9	187.8	-828.9	-1647.9
2002	-132.9	-54.3	-57.6	-139.8	-106.7	90.2	117.6	158.0	47.6	-144.3	-186.0	-304.2	-244.8	-156.3	323.2	-634.5	-712.4
<b>Trade balance, (FOB), million USD</b>																	
2003	-71.3	-121.3	-117.6	-267.0	-287.3	-159.2	-207.8	-159.1	-148.6	-249.6	-322.0	-363.0	-310.2	-713.5	-515.5	-934.6	-2473.8
2002	-82.5	-75.3	-94.2	-148.5	-190.0	-74.0	-82.4	-56.4	-81.9	-174.4	-209.9	-325.0	-252.0	-412.5	-220.7	-709.3	-1594.5



# ANNEX 1: MAIN INDICATORS FOR THE FOURTH QUARTER OF 2003

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
<b>Exports (FOB), million USD</b>																	
2003	544.2	538.7	642.9	570.6	568.0	657.0	717.6	618.1	651.7	677.0	634.3	618.4	1 725.8	1 795.6	1 987.4	1 929.7	7 438.5
2002	383.8	408.8	408.1	425.5	402.9	496.4	586.3	525.8	527.8	520.5	527.8	478.4	1 200.7	1 324.8	1 639.9	1 526.7	5 692.1
<b>Imports (FOB), million USD</b>																	
2003	615.5	660.0	760.5	837.6	855.3	816.2	925.4	777.2	800.3	926.6	956.3	981.4	2 036.0	2 509.1	2 502.9	2 864.3	9 912.3
2002	466.3	484.1	502.3	574.0	592.9	570.4	668.7	582.2	609.7	694.9	737.7	803.4	1 452.7	1 737.3	1 860.6	2 236.0	7 286.6
<b>Services, net, million USD</b>																	
2003	-21.6	-14.0	-24.2	-35.0	29.4	159.7	230.7	237.1	123.6	-21.8	-46.0	-43.4	-59.8	154.1	591.4	-111.2	574.5
2002	-8.4	5.2	-1.2	-34.9	48.0	140.8	202.1	194.3	103.3	-11.4	-23.0	-21.1	-4.4	153.9	499.7	-55.5	593.7
<b>Income, net, million USD</b>																	
2003	-114.3	-48.1	-19.6	-132.9	-13.6	-27.9	-61.5	-4.8	-39.1	11.8	13.8	-2.6	-182.0	-174.4	-105.4	23.0	-438.8
2002	-66.3	-10.6	0.3	5.2	-16.5	-24.3	-87.7	-8.3	-14.6	-10.0	-1.6	-26.6	-76.6	-35.6	-110.6	-38.2	-261.0
<b>Current transfers, net, million USD</b>																	
2003	41.1	27.8	67.9	46.6	45.1	50.3	64.8	72.3	80.1	49.3	53.7	90.8	136.8	142.0	217.2	193.8	689.8
2002	24.2	26.5	37.5	38.5	51.8	47.7	85.5	28.4	40.9	51.4	48.4	68.6	88.2	138.0	154.8	168.4	549.4
<b>Capital account, million USD</b>																	
2003	0.0	0.0	0.0	0.0	0.0	0.0	0.0	-0.1	-0.1	-0.1	0.0	0.0	0.0	0.0	-0.2	-0.1	-0.3
2002	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Financial account, million USD</b>																	
2003	-9.3	81.4	120.4	539.5	220.1	118.6	-52.4	53.8	69.1	489.8	194.5	144.8	192.5	878.2	70.5	829.1	1970.3
2002	76.0	43.2	86.7	311.5	415.7	150.9	-128.5	12.5	129.0	200.5	214.0	211.7	205.9	878.1	13.0	626.2	1723.2
<b>Direct investment abroad, million USD</b>																	
2003	-0.5	-0.4	-1.6	-2.6	0.7	-2.2	-1.9	-4.8	-2.0	-2.9	-0.5	-1.3	-2.5	-4.1	-8.7	-4.7	-20.0
2002	-0.1	-0.2	-0.2	-0.3	-0.1	-0.6	-0.9	-1.9	-0.2	-1.3	-0.2	-22.6	-0.5	-1.0	-3.0	-24.1	-28.6
<b>Direct investment in Bulgaria, million USD</b>																	
2003	86.5	65.6	127.2	148.3	188.6	102.6	164.0	74.7	74.5	310.3	-18.7	37.2	279.3	439.5	313.2	328.8	1360.8
2002	50.2	61.7	107.6	121.0	230.7	6.8	-6.6	33.0	31.8	130.7	55.4	82.3	219.5	358.5	58.2	268.4	904.6
<b>Portfolio investment assets, million USD</b>																	
2003	13.0	10.0	-19.9	10.5	86.5	-36.6	-87.2	-55.3	28.2	-36.7	24.7	-10.1	3.1	60.4	-114.3	-22.1	-72.9
2002	44.3	-71.6	-73.2	81.3	65.6	102.2	16.2	-17.4	7.5	-34.2	88.7	15.7	-100.5	249.1	6.3	70.2	225.1
<b>Portfolio investment liabilities, million USD</b>																	
2003	-32.0	-3.3	-29.8	0.4	30.2	-1.4	-87.9	-16.1	10.2	-14.8	5.6	4.4	-65.1	29.2	-93.8	-4.8	-134.5
2002	-18.8	-15.8	-36.8	-100.7	-23.1	-50.2	-85.5	14.7	18.0	-17.3	29.8	-16.3	-71.4	-174.0	-52.8	-3.8	-302.0
<b>Other investment assets, million USD</b>																	
2003	-15.1	34.7	-60.0	256.7	-140.0	-36.4	-47.2	96.4	-141.6	163.5	88.9	-48.3	-40.4	80.3	-92.4	204.1	151.6
2002	4.4	90.8	15.4	183.5	71.1	-18.5	-98.6	-25.7	10.1	107.3	7.5	-64.4	110.6	236.1	-114.2	50.4	282.9
<b>Other investment liabilities, million USD</b>																	
2003	-61.1	-25.1	104.5	126.2	54.1	92.6	7.7	-41.0	99.8	70.4	94.5	162.9	18.3	272.9	66.5	327.8	685.5
2002	-4.1	-21.7	73.9	26.6	71.4	111.2	46.9	9.9	61.8	15.3	32.7	217.0	48.1	209.2	118.6	265.0	640.9

# ANNEX 1: MAIN INDICATORS FOR THE FOURTH QUARTER OF 2003

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
<b>Net Errors and Omissions (BP), million USD</b>																	
2003	-124.5	119.3	55.3	23.8	111.3	-73.5	24.5	-79.7	-10.4	51.7	214.4	98.0	50.1	61.6	-65.6	364.1	410.2
2002	-174.9	0.7	-96.8	-31.5	-210.8	-27.5	48.7	-73.4	-32.8	84.5	82.6	135.8	-271.0	-269.8	-57.5	302.9	-295.4
<b>Overall balance (BP), million USD</b>																	
2003	-299.8	45.1	82.3	175.1	104.9	67.8	-1.6	119.5	74.7	331.1	108.4	-75.4	-172.4	347.8	192.6	364.1	732.1
2002	-231.8	-10.4	-67.7	140.1	98.2	213.6	37.8	97.0	143.8	140.7	110.6	43.3	-309.9	451.9	278.6	294.6	715.2
<b>Reserves and Related Items, million USD</b>																	
2003	299.8	-45.1	-82.3	-175.1	-104.9	-67.8	1.6	-119.5	-74.7	-331.1	-108.4	75.4	172.4	-347.8	-192.6	-364.1	-732.1
2002	231.8	10.4	67.7	-140.1	-98.2	-213.6	-37.8	-97.0	-143.8	-140.7	-110.6	-43.3	309.9	-451.9	-278.6	-294.6	-715.2
<b>Finance</b>																	
<b>Financial indicators</b>																	
<b>Exchange rate BGN / USD, average for the period</b>																	
2003	1.84170	1.81554	1.81026	1.80353	1.68361	1.67717	1.72003	1.75641	1.74550	1.67286	1.67178	1.59306	1.82250	1.72144	1.74065	1.64590	1.73262
2002	2.21474	2.24804	2.23369	2.20959	2.13121	2.04781	1.97152	2.00039	1.99537	1.99354	1.95327	1.92447	2.23216	2.12954	1.98909	1.95709	2.07697
<b>Exchange rate BGN / USD, end of the period</b>																	
2003	1.80827	1.81393	1.79516	1.75710	1.65440	1.71159	1.72807	1.78991	1.67854	1.68287	1.63067	1.54856	1.79516	1.71159	1.67854	1.54856	1.54856
2002	2.26448	2.26081	2.24190	2.17121	2.08355	1.96073	1.99921	1.98905	1.98360	1.98280	1.97021	1.88496	2.24190	1.96073	1.98360	1.88496	1.88496
<b>Basic interest rate, effective annual, average for the period</b>																	
2003	3.27	2.53	2.55	2.60	2.98	2.92	2.54	2.55	2.59	2.62	2.63	2.69	2.78	2.83	2.56	2.65	2.71
2002	4.86	4.66	4.52	4.16	3.98	3.79	3.72	3.82	3.81	3.76	3.76	3.39	4.68	3.98	3.78	3.64	4.02
<b>Money (M1), BGN million</b>																	
2003	5 141.2	5 235.0	5 087.1	5 272.3	5 371.4	5 583.0	5 789.0	6 054.3	6 060.9	6 044.1	6 128.4	6 801.0	5 087.1	5 583.0	6 060.9	6 801.0	6 801.0
2002	4 651.4	4 584.3	4 594.2	4 602.9	4 474.8	4 402.9	4 589.0	4 750.4	4 804.9	4 804.1	4 936.0	5 542.7	4 594.2	4 402.9	4 804.9	5 542.7	5 542.7
<b>Money (M2), BGN million</b>																	
2003	13 239.4	13 388.3	13 156.3	13 401.7	13 415.1	13 867.7	14 252.3	14 683.9	14 714.6	15 367.0	15 286.7	16 054.5	13 156.3	13 867.7	14 714.6	16 054.5	16 054.5
2002	12 035.3	12 068.5	12 088.1	12 136.0	11 902.6	11 875.7	12 243.5	12 521.5	12 589.7	12 703.6	12 929.4	13 581.3	12 088.1	11 875.7	12 589.7	13 581.3	13 581.3
<b>International reserves of BNB, BGN million</b>																	
2003	8 363.2	8 472.8	8 602.7	9 233.3	9 315.7	9 451.3	9 517.7	9 799.7	9 881.9	10 413.4	10 556.8	10 382.8	8 602.7	9 451.3	9 881.9	10 382.8	10 382.8
2002	7 372.4	7 373.0	7 196.2	7 427.8	7 546.3	7 908.4	8 034.3	8 231.8	8 496.2	8 750.6	8 923.6	8 947.5	7 196.2	7 908.4	8 496.2	8 947.5	8 947.5
<b>Fiscal reserves at the Issue Department of BNB, BGN million</b>																	
2003	2 793.2	2 803.8	3 027.5	3 632.7	3 873.1	3 747.4	3 766.3	3 767.3	3 831.5	3 970.8	4 176.6	3 280.1	3 027.5	3 747.4	3 831.5	3 280.1	3 280.1
2002	2 276.2	2 260.4	2 106.5	2 358.9	2 803.3	3 020.8	3 065.5	3 108.2	3 238.9	3 482.0	3 685.8	3 034.7	2 106.5	3 020.8	3 238.9	3 034.7	3 034.7
<b>Banking system</b>																	
<b>Claims on credits granted by the Commercial Banks, total, BGN thousand</b>																	
2003	6 444 818	6 563 130	6 816 766	7 167 024	7 424 452	7 727 590	7 866 307	8 171 994	8 471 157	8 904 325	9 114 301	9 454 164	6 816 766	7 727 590	8 471 157	9 454 164	9 454 164
2002	4 520 277	4 543 750	4 609 974	4 796 653	4 944 889	5 065 015	5 352 435	5 512 677	5 765 237	5 923 656	6 126 486	6 409 070	4 609 974	5 065 015	5 765 237	6 409 070	6 409 070
<b>Credits to Resident Sector, total</b>																	
2003	6 356 088	6 489 721	6 745 467	7 094 504	7 355 881	7 657 439	7 797 284	8 092 008	8 391 057	8 832 873	9 044 229	9 352 878	6 745 467	7 657 439	8 391 057	9 352 878	9 352 878
2002	4 472 243	4 507 846	4 573 470	4 760 548	4 893 417	5 016 555	5 300 222	5 453 859	5 689 755	5 822 181	6 016 990	6 316 911	4 573 470	5 016 555	5 689 755	6 316 911	6 316 911

# ANNEX 1: MAIN INDICATORS FOR THE FOURTH QUARTER OF 2003

(Continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
<b>Credits to Government Sector</b>																	
2003	8 673	8 947	9 494	9 380	9 406	9 561	11 924	13 394	19 928	21 667	22 168	24 635	9 494	9 561	19 928	24 635	24 635
2002	5 066	6 350	6 932	6 669	6 933	6 512	6 196	9 203	9 404	9 391	9 536	8 486	6 932	6 512	9 404	8 486	8 486
<b>Credits to Non-government Sector</b>																	
2003	6 291 902	6 444 260	6 662 763	7 014 528	7 280 799	7 603 463	7 727 111	8 030 421	8 325 688	8 751 119	8 977 126	9 303 120	6 662 763	7 603 463	8 325 688	9 303 120	9 303 120
2002	4 439 405	4 487 627	4 552 367	4 736 963	4 857 929	4 971 905	5 256 205	5 399 240	5 639 343	5 772 922	5 977 063	6 250 741	4 552 367	4 971 905	5 639 343	6 250 741	6 250 741
<b>Credits to Non-financial Public Corporations</b>																	
2003	219 215	229 954	235 631	246 234	245 746	231 489	245 251	237 021	230 292	213 420	217 489	234 230	235 631	231 489	230 292	234 230	234 230
2002	183 596	175 571	180 510	225 524	222 297	211 154	211 675	208 075	195 975	202 831	207 660	215 935	180 510	211 675	195 975	215 935	215 935
<b>Credits to Non-financial Private Corporations</b>																	
2003	4 715 900	4 800 569	4 949 708	5 202 209	5 377 904	5 604 204	5 575 897	5 774 664	5 956 901	6 287 344	6 412 770	6 641 717	4 949 708	5 604 204	5 956 901	6 641 717	6 641 717
2002	3 339 231	3 380 809	3 416 763	3 521 944	3 614 751	3 702 339	3 941 157	4 040 047	4 235 802	4 315 476	4 459 918	4 700 997	3 416 763	3 702 339	4 235 802	4 700 997	4 700 997
<b>Credits to Households</b>																	
2003	1 260 492	1 300 531	1 355 108	1 438 127	1 532 501	1 645 779	1 758 072	1 853 587	1 933 809	2 035 462	2 116 719	2 201 298	1 355 108	1 645 779	1 933 809	2 201 298	2 201 298
2002	864 317	879 057	900 932	933 388	955 478	993 405	1 035 501	1 079 306	1 126 596	1 172 289	1 214 409	1 241 560	900 932	993 405	1 126 596	1 241 560	1 241 560
<b>Credits to Non-bank Financial Institutions</b>																	
2003	96 295	113 206	122 316	127 958	124 648	121 991	147 891	165 149	204 686	214 893	230 148	225 875	122 316	121 991	204 686	225 875	225 875
2002	52 261	52 190	54 162	56 107	65 403	65 007	67 872	71 812	80 970	82 326	95 076	92 249	54 162	65 007	80 970	92 249	92 249
<b>Credits to Resident Banks</b>																	
2003	55 513	36 514	73 210	70 596	65 676	44 415	58 249	48 193	45 441	60 087	44 935	25 123	73 210	44 415	45 441	25 123	25 123
2002	27 772	13 869	14 171	16 916	28 555	38 138	37 821	45 416	41 008	39 868	30 391	57 684	14 171	38 138	41 008	57 684	57 684
<b>Credits to Non-resident Sector</b>																	
2003	88 730	73 409	71 299	72 520	68 571	70 151	69 023	79 986	80 100	71 452	70 072	101 286	71 299	70 151	80 100	101 286	101 286
2002	48 034	35 904	36 504	36 105	51 472	48 460	52 213	58 818	75 482	101 475	109 496	92 159	36 504	48 460	75 482	92 159	92 159
<b>Total assets, end of the period, BGN thousand</b>																	
2003	14 470 798	14 527 980	14 976 602	14 754 441	14 752 332	15 359 751	15 706 435	16 019 647	16 386 230	16 621 238	16 608 301	17 323 643	14 976 602	15 359 751	16 386 230	17 323 643	17 323 643
2002	12 340 044	12 286 166	12 710 381	12 722 090	12 473 976	12 394 798	12 924 968	13 225 015	13 475 455	13 503 015	13 901 329	14 557 124	12 710 381	12 394 798	13 475 455	14 557 124	14 557 124
<b>Total liabilities, end of the period, BGN thousand</b>																	
2003	12 413 277	12 474 347	12 882 639	12 702 089	12 694 628	13 252 494	13 584 220	13 870 342	14 218 293	14 410 754	14 364 457	15 042 658	12 882 639	13 252 494	14 218 293	15 042 658	15 042 658
2002	10 676 646	10 602 225	11 014 662	11 040 181	10 782 330	10 682 602	11 197 870	11 455 975	11 681 572	11 674 854	12 053 348	12 621 459	11 014 662	10 682 602	11 681 572	12 621 459	12 621 459
<b>Interest revenues, BGN thousand</b>																	
2003	74 730	145 393	223 314	302 382	385 403	465 864	550 315	636 814	724 416	816 202	908 081	1 012 487	223 314	465 864	724 416	1 012 487	1 012 487
2002	56 711	110 773	168 685	224 465	283 518	342 850	405 735	468 644	533 137	600 091	672 166	738 092	168 685	342 850	533 137	738 092	738 092
<b>Current profit/loss, BGN thousand</b>																	
2003	98 482	122 770	125 420	148 232	180 278	218 487	242 268	266 588	293 663	322 514	355 375	379 817	125 420	218 487	293 663	379 817	379 817
2002	25 913	47 270	56 996	80 116	112 082	132 715	148 229	182 185	201 740	240 089	258 199	266 625	56 996	132 715	201 740	266 625	266 625

# ANNEX 1: MAIN INDICATORS FOR THE FOURTH QUARTER OF 2003

(Continued)													Year
Social policy and industrial relations													
Wage&Salary 1)													
Average Monthly Wage&Salary of employees under labor contract, total, nominal, BGN													
2003	270	265	280	272	280	274	276	273	286	276	286	302	278
2002	251	252	265	262	269	265	267	265	272	271	272	282	266
Average Monthly Wage&Salary of employees under labor contract, public sector, nominal, BGN													
2003	308	299	325	318	340	327	326	324	352	326	344	368	330
2002	282	285	304	298	318	311	309	312	328	321	319	332	310
Average Monthly Wage&Salary of employees under labor contract, private sector, nominal, BGN													
2003	238	234	242	244	242	241	244	242	245	245	249	260	244
2002	229	229	238	238	236	235	240	236	237	240	241	249	237
Real Average Monthly Wage&Salary of employees under labor contract, total, growth, corresponding period of the previous year =100, %													
2003	5.7	4.9	5.8	3.6	2.3	2.1	1.3	-0.5	1.4	-1.5	0.1	1.4	2.2
2002	1.6	2.0	1.6	-3.3	-0.9	-0.8	1.6	2.3	2.2	3.8	3.4	0.6	1.1
Real Average Monthly Wage&Salary of employees under labor contract, public sector, growth, corresponding period of the previous year =100, %													
2003	7.3	4.7	7.1	6.4	5.1	3.8	3.4	0.3	3.5	-1.6	4.5	6.8	4.0
2002	2.6	3.5	2.8	-2.9	-0.8	0.2	2.1	5.2	2.8	8.3	5.5	1.2	2.4
Real Average Monthly Wage&Salary of employees under labor contract, private sector, growth, corresponding period of the previous year =100, %													
2003	2.1	1.9	1.8	2.3	0.8	1.3	-0.4	-0.9	-0.3	-1.1	0.1	0.6	0.4
2002	1.4	1.6	1.9	-2.3	-0.6	-0.7	2.5	0.8	3.1	1.1	2.0	0.8	0.9
Income and consumption of the households 1)													
Total income, monthly, average per person, nominal, BGN													
2003	128.8	122.4	135.8	142.4	146.6	152.3	157.2	157.0	157.0	156.2	162.1	210.6	152.4
2002	113.4	113.2	126.5	130.6	136.6	135.3	137.3	142.7	148.5	146.7	144.1	195.5	139.2
Cash income, monthly, average per person, nominal, BGN													
2003	124.5	118.3	130.2	132.5	134.2	139.1	142.2	142.0	142.2	140.7	137.2	175.3	138.2
2002	109.3	109.6	120.9	122.0	123.1	123.5	124.8	128.7	135.5	132.2	126.3	157.0	126.1
Total expenditure, monthly, average per person, nominal, BGN													
2003	125.2	116.0	130.1	135.5	143.2	141.9	147.1	151.1	153.1	154.9	153.4	197.9	145.8
2002	109.4	112.0	120.3	124.1	136.4	130.6	133.6	140.8	147.6	143.6	141.6	183.8	135.3
Cash expenditure, monthly, average per person, nominal, BGN													
2003	121.1	112.3	124.9	126.0	131.4	129.7	133.2	137.0	139.3	140.4	135.0	163.6	132.8
2002	105.5	108.6	114.9	115.6	123.2	118.9	121.2	127.0	134.9	129.8	124.2	146.3	122.5
Real total income, monthly, average per person, growth, corresponding period of the previous year =100, %													
2003	11.6	7.9	7.5	8.7	5.5	11.1	12.2	6.3	2.0	3.0	7.0	2.0	6.9
2002	0.1	5.3	3.3	1.7	4.5	5.2	5.2	8.5	12.6	12.7	10.2	23.4	8.0



# ANNEX 1: MAIN INDICATORS FOR THE FOURTH QUARTER OF 2003

(Continued and end)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
Real cash income, monthly, average per person, growth, corresponding period of the previous year =100, %																	
2003	11.9	7.7	7.8	8.3	7.1	11.2	11.7	6.6	1.3	2.9	3.4	5.7	9.1	8.9	6.4	4.2	7.1
2002	0.6	5.2	3.7	2.5	3.8	5.0	5.3	8.5	13.5	12.1	9.2	20.3	3.2	3.7	9.1	14.2	7.6
Real total expenditure, monthly, average per person, growth, corresponding period of the previous year =100, %																	
2003	12.4	3.3	8.3	8.9	3.1	7.3	7.9	3.7	0.1	4.3	3.1	1.9	8.0	6.4	3.8	3.1	5.2
2002	-2.5	8.3	2.9	-0.3	5.3	7.7	5.5	9.8	12.3	11.5	12.5	20.2	2.8	4.2	9.3	15.1	8.0
Real cash expenditure, monthly, average per person, growth, corresponding period of the previous year =100, %																	
2003	12.8	3.1	8.9	8.6	4.8	7.7	7.7	4.3	-0.4	4.6	3.4	5.9	8.2	7.0	3.7	4.7	5.9
2002	-2.1	8.5	3.4	0.4	4.5	7.8	5.9	9.9	13.3	11.2	12.1	16.9	3.1	4.2	9.7	13.5	7.7

1) Average monthly values by quarter are calculated as simple average of monthly per capita values.

Sources: Employment Agency, Bulgarian National Bank, Ministry of Finance, National Statistical Institute and own calculations.

Acronyms:

GDP = Gross domestic product

" - " = Not applicable or missing data

## ANNEX 2: REGULATORY DOCUMENTS PROMULGATED IN THE FOURTH QUARTER OF 2003

Title	Status	Official Gazette
ORDINANCE on the terms and procedure of changing the participation or transferring the accumulated funds of an insured person from one supplementary pension insurance fund to another corresponding fund managed by another pension insurance company	New	No. 90/10.10.2003
ORDINANCE on the requirements for the activity of investment brokers	New	No. 90/10.10.2003
ORDINANCE on the offering circulars in the public offering of securities and on the disclosure of information by public companies and by the other issuers of securities	New	No. 90/10.10.2003
ACT on the ratification of the Information Access Convention, the participation of the society in the decision-making process, and the access to justice for environmental issues	New	No. 91/14.10.2003
ORDINANCE on the social security of self-insured persons and of Bulgarian citizens working abroad	Amended	No. 91/14.10.2003
ACT on the promotion of scientific research	New	No. 92/17.10.2003
Local Elections ACT	Amended	No. 93/21.10.2003
ORDINANCE on the rates of admissible emissions (concentrations in waste gases) to the air of harmful substances from stationary sources	Amended	No. 93/21.10.2003
ORDINANCE on the terms and procedure of measuring the emissions to the air of harmful substances from stationary sources	Amended	No. 93/21.10.2003
ORDINANCE on the rates of admissible emissions (concentrations in waste gases) to the air of sulfur dioxide, nitric oxide and dust from large combustion plants	Amended	No. 93/21.10.2003
ORDINANCE on determining the procedure for establishing the availability of the criteria for representativeness of the workers and employees' organizations and of employers .	Amended	No. 93/21.10.2003
ORDINANCE on the protection of employed persons against risks of exposure to carcinogens and mutagens at work	New	No. 94/24.10.2003
Personal Income Taxation ACT	Amended	No. 95/28.10.2003
Customs Office ACT	Amended	No. 95/28.10.2003
Public Servant ACT	Amended	No. 95/28.10.2003
Administration ACT	Amended	No. 95/28.10.2003
Labor CODE	Amended	No. 95/28.10.2003
Social Security CODE	Amended	No. 95/28.10.2003
ORDINANCE on determining the list of illnesses for which treatment at home shall be fully or partially payable by NHIF	Amended	No. 96/31.10.2003
ORDINANCE on the rates of admissible emissions to the air of volatile organic compounds as a result of the use of solvents in certain plants	Amended	No. 96/31.10.2003
CoM's DECREE No. 237/ 24.10.2003 on the allocation of single subsidy from the state budget for 2003 to support commercial companies	Amended	No. 96/31.10.2003
ORDINANCE on the terms and procedure of paying export subsidies for the export of agricultural products	New	No. 97/4.11.2003
Road Transport ACT	Amended	No. 99/11.11.2003
ORDINANCE on the terms and procedure of issuing licenses to consultants for assessment of the compliance of investment projects and/or for carrying out building supervision	New	No. 99/11.11.2003
ORDINANCE on food labeling and presentation requirements	Amended	No. 100/14.11.2003
ADDITIONAL PROTOCOL No. 13 to the Central European Free Trade Agreement	New	No. 100/14.11.2003
ORDINANCE on the capital adequacy and liquidity of investment brokers	New	No. 101/18.11.2003
ORDINANCE on determining basic prices, prices of excluded areas, and on the right of use and servitude on forests and land from the forestry fund	New	No. 101/18.11.2003

## ANNEX 2: REGULATORY DOCUMENTS PROMULGATED IN THE FOURTH QUARTER OF 2003

Title	Status	Official Gazette
ORDINANCE on the production of and trade in vegetable crop seeds	New	No. 101/18.11.2003
ORDINANCE on the accounting and the budget of the syndic of a bank in bankruptcy	New	No. 102/21.11.2003
CIVIL CONVENTION on corruption		No. 102/21.11.2003
ORDINANCE on the cryptographic security of classified information	New	No. 102/21.11.2003
ORDINANCE on the production of and trade in cereal crop seeds	New	No. 102/21.11.2003
Foods ACT	Amended	No. 102/21.11.2003
Public Health ACT	Amended	No. 102/21.11.2003
Medical Institutions ACT	Amended	No. 102/21.11.2003
ORDINANCE on the terms and procedure of the State's participation in the payment of the "water supply" service	Amended	No. 103/25.11.2003
Foreigners in the Republic of Bulgaria ACT	Amended	No. 103/25.11.2003
Political Parties ACT	Amended	No. 103/25.11.2003
Excise Duty ACT	Amended	No. 103/25.11.2003
ORDINANCE on the criteria, indicators and methods of accreditation of medical institutions	Amended	No. 105/2.12.2003
Territorial Development ACT	Amended	No. 107/9.12.2003
ACT on the technical requirements for products	Amended	No. 107/9.12.2003
ACT on the restriction of the administrative regulation and administrative control of the economic activity	Amended	No. 107/9.12.2003
Municipal Budgets ACT	Amended	No. 107/9.12.2003
Competition Protection ACT	Amended	No. 107/9.12.2003
Energy ACT	New	No. 107/9.12.2003
Energy and Energy Efficiency ACT	Amended	No. 107/9.12.2003
Forestry ACT	Amended	No. 107/9.12.2003
Waters ACT	Amended	No. 107/9.12.2003
ACT on the 2003 budget of the National Health Insurance Fund	Amended	No. 107/9.12.2003
ORDINANCE on the internal control in banks	New	No. 108/12.12.2003
ORDINANCE on the licenses and permits issued by the Bulgarian National Bank	New	No. 108/12.12.2003
ORDINANCE on the Central Depositary of Securities	New	No. 108/12.12.2003
ORDINANCE on the requirements for the composition and the structure of the equity capital (capital base) of the pension insurance company and for the minimum liquid assets of the company and the supplementary pension insurance funds managed by the company	New	No. 109/16.12.2003
Value Added Tax ACT	Amended	No. 109/16.12.2003
Special Investment Purpose Companies ACT	Amended	No. 109/16.12.2003
Corporate Income Taxation ACT	Amended	No. 109/16.12.2003
Public Procurement ACT	Amended	No. 109/16.12.2003
ORDINANCE on the permits to carry out activity as stock exchange, organizer of unofficial securities market, investment broker, investment company, managing company and special investment purpose company	New	No. 109/16.12.2003
ORDINANCE on the terms and procedure of valuating the assets and liabilities of supplementary pension insurance funds and of the pension insurance company, of assessing the value of the fund's net assets, and of calculating and announcing the value of a share, as well as on the requirements for keeping of the individual lots	New	No. 109/16.12.2003

## ANNEX 2: REGULATORY DOCUMENTS PROMULGATED IN THE FOURTH QUARTER OF 2003

Title	Status	Official Gazette
ORDINANCE on the terms and procedure of determining the minimum yield in the management of supplementary pension insurance funds' assets, of covering the difference up to the minimum yield, and of forming and utilizing the reserves for guaranteeing the minimum yield	New	No. 110/19.12.2003
ORDINANCE on the lending to banks in BGN against collateral	Amended	No. 110/19.12.2003
ORDINANCE on the minimum required reserves maintained by banks with BNB	Amended	No. 110/19.12.2003
ORDINANCE on the balance of payments statistics	Amended	No. 111/22.12.2003
ACT on the 2004 budget of the State Social Security	New	No. 112/23.12.2003
ORDINANCE on determining the basic package of health services guaranteed by NHIF's budget	New	No. 112/23.12.2003
Personal Income Taxation ACT	Amended	No. 112/23.12.2003
Financial Supervision Commission ACT	Amended	No. 112/23.12.2003
ACT on the purity of atmospheric air	Amended	No. 112/23.12.2003
Judiciary ACT	Amended	No. 112/23.12.2003
Farm Land Preservation ACT	Amended	No. 112/23.12.2003
Social Security CODE	Amended	No. 112/23.12.2003
Local Taxes and Charges ACT	Amended	No. 112/23.12.2003
Excise Duty ACT	Amended	No. 112/23.12.2003
ORDINANCE on determining a positive list of medicines in the Republic of Bulgaria	New	No. 113/29.12.2003
ACT on the 2004 state budget of the Republic of Bulgaria	New	No. 114/30.12.2003
Tax Procedure CODE	Amended	No. 114/30.12.2003
Employment Promotion ACT	Amended	No. 114/30.12.2003
National Revenues Agency ACT	Amended	No. 114/30.12.2003
Health and Safety at Work ACT	Amended	No. 114/30.12.2003
Health Insurance ACT	Amended	No. 114/ 30.12.2003
ACT on the budget of the National Health Insurance Fund	New	No. 114/30.12.2003



## ANNEX 3: STATUS OF THE NEGOTIATION CHAPTERS OF BULGARIA'S EU ACCESSION

Chapter	Status (31 December 2003)
1 Free Movement of Goods	Temporarily closed
2 Free Movement of Persons	Temporarily closed
3 Freedom to Provide Services	Temporarily closed
4 Free Movement of Capital	Temporarily closed
5 Company Law	Temporarily closed
6 Competition Policy	Open
7 Agriculture	Open
8 Fishery	Temporarily closed
9 Transport Policy	Temporarily closed
10 Tax Policy	Temporarily closed
11 Economic and Monetary Union	Temporarily closed
12 Statistics	Temporarily closed
13 Social Policy	Temporarily closed
14 Energy	Temporarily closed
15 Industrial Policy	Temporarily closed
16 Small and Medium-sized Enterprises	Temporarily closed
17 Science and Research	Temporarily closed
18 Education and Training	Temporarily closed
19 Telecommunications	Temporarily closed
20 Culture and Audiovision	Temporarily closed
21 Regional Policy	Open
22 Environment	Temporarily closed
23 Consumer Protection	Temporarily closed
24 Justice and Home Affairs	Temporarily closed
25 Customs Union	Temporarily closed
26 Foreign Relations	Temporarily closed
27 Common Foreign and Security Policy	Temporarily closed
28 Fiscal Control	Temporarily closed
29 Fiscal and Budgetary Issues	Open
30 Institutions	Temporarily closed
<b>Total chapters closed</b>	<b>26</b>

## A. GENERAL NOTES

The review of the Bulgarian economy is an authentic expert product of the Center for Economic Development, made possible mostly owing to the long experience of the Center in the field of applied studies of the economic policy and economic development of the country.

The present report on the Bulgarian economy follows the structure and content of the review established after the report on the second quarter of 2003. The objective of the changes was to satisfy users' interest and to establish the publication as a source of reliable and comprehensive information about the economic development and the economic policy in the past quarters.

The review of the Bulgarian economy in the fourth quarter of 2003 contains detailed presentation of the review period, assessment of the period and subsequent trends. The review is explicitly focused on this quarter of the current year. Where necessary, significant events, facts and data of periods prior to or after the end of the quarter have been highlighted. Where possible, two main types of data comparisons have been made: against the corresponding period of 2002 or against the previous quarter of 2003. Again where possible, the dynamics within the quarter itself has been traced, too. At many points also the short-term trend has been outlined.

The structure of the presentation above follows two principles simultaneously. First, the strive is towards giving a more comprehensive presentation of the subject matter areas, with corresponding prioritization of the range of matters discussed. Second, the different topics and analyses reflect the experience and interests of the experts and of the Center for Economic Development as a whole.

The review of Bulgaria's economy in the fourth quarter of 2003 starts with presentation of the macroeconomic dynamics discussed against the background of the following basic categories: GDP, inflation, employment and unemployment, balance of payments, foreign trade and foreign direct investments. After that the latest values of the Estat index of business climate in Bulgaria are presented and compared. The national economic events in the reviewed quarter, which have direct or indirect effect on the competitiveness of the Bulgarian enterprises, are analyzed in the new section on the enterprise policy. Such events are described in the sub-sections on condition of the entrepreneurial environment, investment promotion policy, administrative and regulatory environment, effectively functioning markets, access to financing, privatization and commercial policy. In the specific Bulgarian economic environment the enterprise policy has two basic aspects – transformational, which is mostly associated with the process of privatization and liberalization of the economy, and competitiveness-oriented, which involves the policies to

achieve economic growth and competitiveness of the Bulgarian enterprises. The corresponding section of the report studies problems concerning both aspects of the Bulgarian enterprise policy.

The public finance section covers the budget implementation and the fiscal reserve dynamics, the credit ratings, the foreign and the domestic debt. The wide topic of social and healthcare policies encompasses the issues of social security, employment and unemployment, labor market policy, income and social partnership. A review is made of the current problems and condition of the healthcare reform. The environmental policy is discussed both as a specific element of the economic policy and as a factor for the economic environment.

The financial sector is discussed by means of the banking system and the capital market. Then comes the review of a number of sectors of significant importance to the economic development of Bulgaria – energy, transport, high technologies and communications, tourism and agriculture. The section on regional economic development studies, so far as that is possible on a quarterly basis, the political decisions, facts and events relating to the achievement of balanced and sustainable development of the regions and reduction of the disproportions between them, as well as the process of social and economic cohesion with the European Union.

A review of the Bulgarian economy in 2003 is presented under the heading "In Focus" of the present report.

The annexes at the end constitute an integral part of the presentation. Annex 1 presents in detail the basic indicators in the quarter under review. Annex 2 contains the list of newly passed legislation and amendments to laws, which are of significant importance to the economic development of the country, and were promulgated in the Official Gazette in the fourth quarter of the year. The last annex (Annex 3) illustrates the status of the EU accession negotiation chapters.

The work was finally completed on 9 March 2004.

## B. SOURCES

Along with the conclusions from a large number of own outputs and works, some of which are parts of concrete research projects, the experts of the Center for Economic Development have used statistical and other information and data from the following basic sources:

- National Assembly
- Council of Ministers
- Ministry of Energy and Energy Resources
- Ministry of Agriculture and Forestry
- Ministry of Economy
- Ministry of Transport and Communications
- Ministry of Labor and Social Policy

- Ministry of Finance
- National Statistical Institute
- National Social Security Institute
- Employment Agency
- Agency for Small and Medium-sized Enterprises
- Privatization Agency
- Bulgarian National Bank
- Bulgarian Stock Exchange – Sofia AD
- Financial Supervision Commission
- Delegation of the European Commission
- European Union
- Eurostat
- European Bank for Reconstruction and Development
- Organization for Economic Cooperation and Development
- Official Gazette

The particular sources and publications are quoted at the respective places in the text.

## C. THE ESTAT INDEX OF BUSINESS CLIMATE IN BULGARIA

The business climate survey is based on own original methodology, developed by the team of the Agency for Social and Marketing Surveys Estat and the Center for Economic Development. The more significant details are described below.

### *Methodology of the Sample*

The survey was conducted in the period 20 – 29 January 2004 among the managers of 409 companies. The sample is a two-level panel one (at the first level the companies are divided into groups by regions, and at the second level – according to their economic sectors as per nomenclature A6 of the NSI), and it is grouped on the basis of the indices “number of employees” and “type of ownership”. The sample is a guaranteed representative one at the level of going concerns.

### *Methodology of the Registration*

The information has been collected using the method of an inquiry at the work place. The interviews were held with the owners of the companies covered by the sample, or with persons authorized to make management decisions and to sign financial statement documents (managers, chief accountants, commercial or marketing directors).

The questionnaire contains eight substantive questions and three passport questions. The integrated index is comprised of three components. The questions from one to five inclusive comprise Component I – “General Condition of the Company”; question six – Component II – “Investment Attitudes and

Corporate Strategies”; questions seven and eight – Component III – “Business Environment”.

### *General Description of the Index Calculation*

#### 1. Preliminary preparation

The preliminary preparation includes weighting of the data according to the indicators “economic sector” and “number of employees”, recoding and calculating values for the respective questions.

- Questions with one possible answer

The original scales are of Likert type with codes from 1 (the highest degree) to 5 (the lowest degree). Recoding is done so as to have a scale from -2 (the lowest degree) to +2 (the highest degree).

- Multiple choice questions

These questions are recoded in advance so that possible answers are located symmetrically on both sides of the neutral point (the zero).

#### 2. Calculation of the components

The index for each question (indicator) is calculated as a weighted average value.

Weights are assigned to each indicator within a component by means of expert evaluation. The value for each component (“General Condition of the Company”; “Investment Attitudes and Corporate Strategies”; “Business Environment”) is calculated as a weighted average.

#### 3. Calculation of an integrated index

The integrated index is calculated as a weighted average of the three components. The weight for each of the components is determined by means of expert evaluation.

The Estat index of business climate assumes values from -100 to +100. The business climate condition is assessed according to the following scale, similar to the one used in the German IFO Business Climate Index:

-100 to -61	very poor
-60 to -21	poor
-20 to +20	average
+21 to +60	good
+61 to +100	very good

### *Interpretation*

All components (with no exception), as well as the integrated index, assume values within the interval [-100, +100]. The set of tools allows to determine also the direction of the index. The

difference between the values of questions Q3 (assessment of the expected condition), Q2 (assessment of the condition at a certain point in time) and Q1 (assessment of the condition during the preceding period) is applied as a criterion for determining the direction.

**Beside everything aforesaid about the methodology, in many places throughout the text additional methodological and other notes and comments are given.**

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## Workshop on Enterprise Policy Issues

A workshop on enterprise policy in Southeast Europe was held on October 2 – 3, 2003 in Istanbul. The workshop was organized by the Investment Compact of the Organization for Economic Cooperation and Development (OECD). The workshop, attended by Ms. Magdalena Varshilova, expert at CED, was organized in cooperation with the EC Enterprise Directorate General and the European Bank for Reconstruction and Development (EBRD).

The workshop was the final phase of the OECD and EBRD regional project Assessment of Enterprise Policy in Southeast Europe. Experts from nine countries, Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Macedonia, Moldova, Romania, Serbia and Montenegro, took part. CED was partner of OECD and EBRD in this project. CED experts contributed in the development of the reports Assessment of Enterprise Policy in Bulgaria and Assessment of Enterprise Policy in Macedonia, as well as in the preparation of the regional report Assessment of Enterprise Policy in Southeast Europe.

The main objective of the Istanbul workshop was to present and discuss the conclusions and recommendations of the reports on the nine countries and of the regional report, on the following six key elements for the development of enterprises:

- Institutional framework of the policy for small and medium-sized enterprises
- Legislative and regulatory environment
- Tax policy regarding small businesses
- Financial instruments for start-up and small businesses
- Advisory services for start-up and small businesses
- Business incubators

## Meeting with Mr. James Roaf



From left to right: A. Boshkov, Co-chair of CED Board of Trustees; J. Roaf, IMF Resident Representative in Bulgaria; G. Prohasky, Co-chair of CED Board of Trustees; V. Spassova, CED Expert

On October 16, 2003, CED management and experts held a meeting with Mr. James Roaf, IMF Resident Representative in Bulgaria. One of the issues discussed was the IMF's position regarding the main parameters of the 2004 budget (incl. the budget deficit for the next year) as well as the condition of the basic macroeconomic indicators. Mr. Roaf stated that despite the macroeconomic stability achieved in the country, Bulgaria should continue to implement a conservative fiscal policy. One of the possible measures in this respect was the fulfillment of the government's commitment for a budget deficit within 0.5 per cent of GDP in 2004 and for achieving a balanced budget in 2005.

In the discussion of the main macroeconomic indicators, Mr. Roaf shared that a substantial progress has been achieved in the stabilization of the economy. Issues of concern are the increasing deficit in the current account of the balance of payments and the significant growth of bank loans over the past year. The CED representatives presented the activity and achievements of the organization to Mr. Roaf.

## Southeast Europe Economic Forum



From right to left: L. Shouleva, Deputy Prime Minister and Minister of Economy; A. Boshkov, Co-chair of CED Board of Trustees; Oscar de Bruyn Kops, Country Manager to Bulgaria, The World Bank; D. Murphy, Program Director, Investment Compact for Southeast Europe, OECD; Alfonso Ferraioli, Adviser, Ministry of Industry and Economy, Italy

CED representatives took part in the 2003 Southeast Europe Economic Forum *Integrating the Southeast Europe Economic Space*, held on November 3 -5, 2003, at the National Palace of Culture. The CED hosted two plenary sessions, *Towards Competitive Southeast Europe: The Role of European Perspective. The Institutional Approach*, and *Competitiveness of the Economies in the Region – Business and Expert Point of View*. Moderator of the first plenary session was the co-chair of CED Board of Trustees, Mr. Alexander Boshkov.

Mrs. Lydia Shouleva, Deputy Prime Minister and Minister of Economy, Republic of Bulgaria, Mrs. Alev Yaraman, Chairman of the Board, Sisecam, Turkey, Mr. Arno Riedel, Director, Department for bi- and multilateral economic relations, Ministry of Foreign Affairs, Austria, Mr. Declan Murphy, Program Director, Investment Compact for Southeast Europe, OECD, Mr. Alfonso Ferraioli, Adviser, Ministry of Industry and Economy, Italy, Mr. Oscar de Bruyn Kops, Country Manager to Bulgaria, The World Bank were the presenters at the first panel.

Mr. Georgi Horozov, Project Finance Manager, Black Sea Trade & Development Bank, moderated the second panel on the Competitiveness of the Economies in the Region – Business and Expert Point of View. The presenters were Mr. Alexander Lamnidis, Executive Director, American-Hellenic Chamber of Commerce, Mrs. Anelia Damianova, Senior Researcher, Center for Economic Development, Mr. James Blewett-Mundy, President, Lion's Bridge, Mr. Marco Montecchi, President, Italian Chamber of Commerce in Bulgaria, Mr. Yann Burtin, Global Information & Communication Technologies Department, The World Bank.



From left to right: A.Damianova, CED Senior Researcher; G.Horozov, Project Finance Manager, Black Sea Trade & Development Bank; A. Lamnidis, Executive Director, American-Hellenic Chamber of Commerce

Mrs. Anelia Damianova from CED presented a report on Bulgaria's Competitiveness in the Area of Information and Communication Technologies. The best achievements of the EU in this area were reviewed together with Bulgaria's positions. A number of best practices for more efficient use of such technologies by entrepreneurs, governments, and individuals, were also presented. Certain recommendations were made to the government and the companies with respect to the use of information and communication technologies as an essential factor for improved competitiveness.

## Meeting of public policy analytical centers in Kiev, Ukraine

On November 7 and 8, 2003, in Kiev, Ukraine, Mr. Ivailo Nikolov, Program Director at CED, took part in the regular workshop of the network of public policy analytical centers, supported by the Open Society Institute, from Eastern Europe and the former Soviet countries.

By tradition, the meeting started with a presentation of the activity of the centers in the period following the spring meeting in London and introduction of new network members. Representatives of the International Public Policy Study Center, which hosted the event, presented in detail the history, activity and structure of the organization. A large portion of the second day of the workshop was dedicated to a discussion of the options for institutionalization of the network of public policy analytical centers. The issues discussed were establishment and registration of an association, statute, membership and funding. Eventually, a working group was set up and a timetable was adopted for implementation of the tasks related to transforming the network of public policy analytical centers in a formal organization.

CED representative gave one of the most important presentations during the meeting in Kiev. The topic was related to the financial condition of the network centers during the past year. The presentation was based on data gathered by CED on the basis of a recently completed project for data collection and analysis of sources of funding and the financial condition of all public policy centers in the region (more than 20 centers) assigned by the Local Governance Initiative in Hungary. The conclusions and recommendations related to the strategies for attracting new financing, especially from sources other than those related to the Open Society Institute, generated significant interest and raised a vivid discussion among the participants in the Kiev meeting.

## Roundtable on heat supply issues

On November, 26, 2003, in NDK, the Ministry of Energy and Energy Resources, with the support of the USAID Open Government Initiative Project, and in cooperation with the Media Development Center, Sofia, organized a roundtable on *Heat Supply – Consumers and Institutions*.

A wide range of heat supply issues were discussed at the roundtable. The competencies of state institutions in the sector and the role of the State Energy Regulatory Commission with

respect to protection of consumer rights and support of the socially underprivileged were also discussed.

Representatives of both the state institutions concerned (MEER, SCER, Ministry of Labor and Social Policy (MLSP)), and the heat supply companies and NGOs took part in the discussion. Mr. Zdravko Ivanov, CED expert, took part in the discussion on the Government Support for the Socially Underprivileged, and summarized the efficiency of the energy benefits offered by government institutions. He also proposed a number of efficiency raising measures geared towards improving the condition of the socially underprivileged.

The roundtable resulted in a summary of the current situation in the sector with respect to each of the topics for discussion. In addition, recommendations to the Government, which would help to improve the condition of consumers and of heat supply as a whole, were formulated.

## Roundtable Protection of Bulgarian Yogurt

Mrs. Marieta Tzvetkovska, Senior Researcher at CED, took part in the roundtable on the possibilities for protection of the name Bulgarian Yogurt (“българско кисело мляко”), organized on December 5, 2003, by the Bulgarian Chamber of Commerce and Industry. The roundtable was attended by representatives of ministries and other institutions concerned with the issue, including the Patent Agency, the Bulgarian Institute for Standardization, the State Agency for Metrology and Technical Supervision, and industrial property experts, milk producers and processors, experts from NGOs.

At the roundtable, CED expert expressed the Center’s position regarding the wide variety of approaches in international relations for protection of products, from geographical location to trademark and patent, and the possibilities for their use. It became clear that Bulgarian yogurt and Bulgarian yogurt yeast are only registered as a geographical name with limited protection. The participants in the discussion set a goal to develop a scheme for protection of Bulgarian yogurt as a product and not only as an appellation of origin. To do that, it would be necessary to prove scientifically that the yeasts isolated in Bulgaria have specific local characteristics and indicators different from the rest. The establishment of a working group was initiated with the task to formulate in detail the measures for protection of the standard for identification of the product *Bulgarian yogurt*. A definition of the product has already been adopted at a recent scientific conference. Now the task is to develop a proposal for an international standard supported with scientific and production arguments, to defend this standard in the EU and to achieve international protection with the support of the Institute for Standardization. This will require the joint efforts of manufacturers, research institutes, the ministries of economy and agriculture, the Patent Agency, and other institutions and organizations. With the right organization and correct actions, this scheme could be applied to other products that need international recognition as a trademark.



## Environmental Justice Initiative

On December 6 and 7, 2003, Mrs. Daniela Petrova, CED expert, took part in a workshop on the project *Environmental Justice in Central and Eastern European Countries*, organized by the Environmental Policy and Law Center within the Central European University in Budapest.

Environmental justice is a term related to every individual's right to live in a clean and safe environment and the cases of disproportionate distribution of the consequences of environmental pollution. The formation of national policies based on this principle is one of the priorities of the EC Sixth Program for Environmental Action and the Sustainable Development Strategy.

The main idea of the Environmental Policy and Law Center was to unite environmental and human rights experts and NGO activists in their efforts to initiate a public debate and to create environment for adequate understanding and application of the environmental justice principle. Subject of analysis under the project will be the importance of factors such as differentiation based on property, social status or ethnic affiliation for creating equality in terms of access to, and consumption of, natural resources. The project is expected to result in increased public awareness of environment protection and environment conditions issues and to create a platform for practical actions for implementation of the environmental justice principle.

## Conference on *European Integration and the Challenges to Economic and Social Synchronization*

On December 10, 2003, in the Sredets Hall of the Sheraton Hotel, the European Institute, the Confederation of Independent Labor Unions of Bulgaria, the Confederation of Labor Podkrepa, the Balkan Institute for Labor and Social Policy, Democracy Foundation, and the Advisory Center for Bulgaria's EU Accession organized a national conference on European Integration and the Challenges to Economic and Social Synchronization. The conference was attended by the chairpersons of the Confederation of Independent Labor Unions of Bulgaria and the Confederation of Labor Podkrepa, Mr. Jeliazgo Hristov and Mr. Konstantin Trenchev, Assoc. Prof. Dr. Lalko Doulevski, chairperson of the Economic and Social Council, Mrs. Yuliana Nikolova, Director of the European Institute, Mrs. Lyubov Panayotova, Program Director of the European Institute, Mr. Ivan Neykov, chairperson of the Managing Board of the Balkan Institute for Labor and Social Policy, Mr. Teodor Dechev, deputy chairperson of the Economic Initiative Union, as well as representatives of government institutions, NGOs, foreign embassies and representative offices, and many journalists.

The co-chair of CED Board of Trustees, Mr. Alexander Boshkov, also presented a report at the conference. He focused on the issue of the level of preparedness of Bulgarian entrepreneurs to participate in the common European market and the role of institutions, government and non-government, to support the adaptation of the companies to the new conditions.

## Meeting with counterparts in Velingrad

On December 12, 2003, the Association Agency for Regional Development – Velingrad organized a Christmas Meeting of Counterparts. The meeting was attended by Mrs. Blenika Djelepova, CED expert, the UNDP Resident Representative, Mr. Neil Buhne, and

representatives of the JOBS Project, the Embassy of Switzerland in Bulgaria, the municipal authorities and the local business.

The joint activities and the events in 2003 were reviewed together with the possibilities to expand the cooperation in 2004.

The CED representative presented the Center's new project, *Attracting the Business for More Efficient Participation in the Fight against Corruption in Velingrad Municipality*, which will be implemented in the period January – September 2004. The project is part of the Civil Society against Corruption Program of Coalition 2000, implemented with the financial support of the USAID.

## Roundtable on Security Policy Issues

On December 16, 2003, at the Sheraton Hotel, Sredets Hall, the Institute for Euro Atlantic Security, the European Institute and the George C. Marshall Association – Bulgaria, organized a roundtable on the topic *The Rightist Reading of the Security Policy in Bulgaria in the beginning of the XXI Century*.

Renown politicians, public figures and journalists took place in the roundtable, including Mr. Vesselin Metodiev, Mr. Stefan Popov, Mr. Boyko Noev, Mr. Velizar Shalamanov, Mrs. Nelly Ognyanova, Mr. Neno Dimov, Mr. Svetoslav Malinov, Mrs. Stoyana Georgieva, Mr. Ivo Tsanev, Mr. Panayot Denev, Mr. Panayot Angarev, Mr. Grozdan Karadjov, Mr. Kiril Valchev, Mr. Kalin Manolov, Mrs. Rumiana Chervenкова, Mr. Yavor Dachkov, Mr. Petar Andonov, Mr. Vassil Garnizov, and others.

CED participated with a report presented by the co-chair of Center's Board of Trustees Mr. Alexander Boshkov. Mr. Boshkov analyzed the level of security of entrepreneurs and investors in Bulgaria in the partially reformed and privatized economy. The report had a special section on the continuous intervention of the government and the attempts to influence economic entities by maintaining full state ownership and monopoly of the enterprises providing services vital for each company, i.e. electricity, water supply, telephone services, heating, roads, ports, railway transport, etc.

## New Publication of the Center for Economic Development

The book *EU Enlargement and Its Impact on the Social Policy and Labor Markets of Accession and Non-accession Countries*, was published in English in December 2003. The book is a result of the regional project *EU Enlargement and Its Impact on the Social Policy and Labor Markets of Accession and Non-accession Countries* implemented with the financial support of Freedom House, Budapest, in the period December 2002 – May 2003.

CED was a project coordinator and the Center for Economic Development in Slovakia, the PRAXIS Center for Policy Studies in Estonia and the Euro-Balkan Institute in FYR Macedonia were project partners.

The publication offers an analysis of the state and development of social policy (employment policy, social insurance policy, social assistance policy and social dialogue development) and labor migration policy in Bulgaria, Slovakia, Estonia and FYR Macedonia. A number of policy

options aimed at reducing the tension and social costs related to the labor migration and free movement of workers as a result of the forthcoming EU enlargement are proposed.

The authors of the book have also studied the impact of the EU labor migration policy on accession and non-accession countries. They also propose a set of measures to reduce possible negative effects on the labor markets after the EU enlargement through transfer of knowledge, experience and skills between NGOs from Bulgaria, Slovakia, Estonia and FYR Macedonia.

